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USAID'S STRENGTHENING PUBLIC FINANCIAL MANAGEMENT IN LATIN AMERICA AND THE CARIBBEAN (PFM-LAC)

Public Financial Management in Subnational Governments of Peru – Loreto and Ucayali

Prepared by: Eduardo Fernandez and Vanessa Ramirez Bowne

October 2014

Contract Number : AID-OAA-I-12-00036/AID-OAA-TO-13-00030

This publication was produced for review by the United States Agency for International Development. It was prepared by Deloitte Consulting LLP.

Strengthening Public Financial Management in Latin America and the Caribbean

Public Financial Management in Subnational Governments of Peru – Loreto and Ucayali

Program Name: USAID Strengthening Public Financial Management in Latin America and the Caribbean (PFM-LAC)

Sponsoring USAID Office: USAID/LAC/RSD/BBEG

Contract Number: AID-OAA-I-12-00036/AID-OAA-TO-13-00030

Contractor: Deloitte Consulting LLP

Date of Publication: October 31, 2014

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This report is made possible by the support of the American people through the United States Agency for International Development (USAID). The contents of this report are the sole responsibility of Deloitte Consulting LLP and its implementing partners and do not necessarily reflect the views of USAID or the United States Government.

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List of Acronyms and Abbreviations

Acronym	Definition
BfR	Budgeting for results
CEPLAN	Spanish acronym for National Center for Strategic Planning (<i>Centro Nacional de Planeamiento Estratégico</i>)
CMMDF	Spanish acronym for Multisectoral Commission for Fiscal Decentralization (<i>Comisión Multisectorial en Materia de Descentralización Fiscal</i>)
GIZ	German Society for International Cooperation (<i>Deutsche Gesellschaft für Internationale Zusammenarbeit</i>)
GoP	Government of Peru
IADB	Inter-American Development Bank
IMF	International Monetary Fund
MEF	Ministry of Economy and Finance
OECD	Organisation for Economic Co-operation and Development
OPI	Planning and Investment Office (<i>Oficina de Programación e Inversiones</i>)
PCM	Presidency of the Council of Ministers (<i>Presidencia del Consejo de Ministros</i>)
PDC	Spanish acronym for Development Plan (<i>Plan de Desarrollo Concertado</i>)
PEDN	Spanish acronym for National Development Plan (<i>Plan Estratégico de Desarrollo Nacional</i>)
PEFA	Public Expenditure and Financial Accountability
PESEM	Spanish acronym for Multiyear Sectoral Strategic Plans (<i>Plan Estratégico Sectorial Multianual</i>)
PFM	Public financial management
PFM-LAC	USAID's Strengthening Public Financial Management in Latin America and the Caribbean project
SECO	Swiss State Secretariat for Economic Affairs – Economic Cooperation and Development
SIAF	Spanish acronym for Integrated Financial Management System (<i>Sistema Integrado de Administración Financiera</i>)
SNIP	Spanish acronym for National Public Investment System (<i>Sistema Nacional de Inversión Pública</i>)
VME	Spanish acronym for Deputy Minister of Economy (<i>Viceministro de Economía</i>)

Acknowledgements

The PFM-LAC team and the report authors would like to extend gratitude to all who supported this project and especially the Peruvian government officials who kindly welcomed the team and provided the bulk of the information contained in this report. Special thanks are extended to Ms. Laura Regio Calderón from the Ministry of Finance for creating the opportunities to interview Ministry officials and for providing the team with invaluable information about the Ministry's efforts to improve its management of public finances. We would like to thank Vice-Minister Carlos Oliva for his time and eagerness to meet with our team.

Thanks to Leonel Diaz, Pedro Naranjo, and Renzo de la Riva for their insights, collection of background information, revisions, and—most importantly—their time. Special appreciation is extended to Eric Uggén for his feedback and insightful guidance. The authors would especially like to thank Ms. Sobeida Gonzales from USAID/Peru and her team for facilitating contacts with the municipalities, helping to coordinate many of the meetings, and providing the authors with access to the required information. Lastly, this report could not have been completed without the assistance of the ProDes project management team and field staff. The authors extend special gratitude to the ProDes Chief of Party Violeta Bermudez and Program Coordinator Cecilia Aldave for providing us with the subnational government contacts, and organizing the team's field visits. Last, but certainly not least, we thank Sonia Rios, Edson Berrios, Carmen Montalvan, and Freddy Vega for all of their uninterrupted support with the interviews, and for spending many hours with our team in discussions over the current state of public financial management in the regions visited.

Executive Summary

In the last decade, Peru has been a regional leader in fiscal sustainability, macroeconomic stability, economic growth, and poverty alleviation. Public financial management (PFM) in Peru has been praised by international organizations, in particular the strong alignment of PFM to support fiscal policy outcomes: fiscal discipline, strategic allocation of resources, and efficient delivery of public services.¹ PFM in Peru includes the institutions, organizations, and systems that regulate and manage public resources within the National Budget. These institutions comprise central, regional, and local (provincial and municipal) government entities, with regional and local governments responsible for managing transferred resources, delivering public services, and achieving results.

This report provides an overview of subnational PFM in Peru and examines subnational PFM institutions and practices in the Amazonian regions of Ucayali and Loreto. It describes strengths and weaknesses and identifies potential areas where technical assistance could strengthen the institutional and organizational capacity of participating entities. The Strengthening Public Financial Management in Latin America and the Caribbean (PFM-LAC) team first conducted desk research and then a field study where the team interviewed over 75 representatives from the Ministry of Economy and Finance (MEF), two regional governments, two provincial governments, seven municipal governments, three subnational government associations in Lima (ANGR, AMPE, and REMURPE),² and various international donor agencies (World Bank, IADB, GIZ, and SECO).³

The main findings from the desk assessment and field interviews include the following:

Planning and Budget Preparation – Subnational governments use tools such as the Integrated Financial Management System (SIAF) and national budget programs (*Programas Presupuestales*) to guide processes and decisions, but there is weak alignment between planning and budgeting. National programs play a prominent role in how subnational governments plan and budget for the priority needs. Subnational governments coordinate less with sectoral ministries and tend to emphasize only those areas that fall within national priorities during the budget process. These issues partially stem from the incomplete decentralization, and the lack of clarity concerning authority and the allocation of resources between the levels of government responsible for the delivery of public goods and services. There are also gaps in the implementation of a results-based budgeting (BfR) framework at the subnational level and in the establishment of a monitoring and evaluation system across the whole of government.

Inter-Governmental Coordination – Peruvian law defines the administrative structures of subnational governments, but does not specify the functions that administrative divisions should perform—a result of the fragmented decentralization in Peru. There are also gaps in coordination mechanisms between the three levels of governments to implement sectoral policies in the territories. Additionally, high personnel

¹ Peru Public Finance Management Report: Based on the Performance Management framework (PEFA). European Union, World Bank, and IADB, 2009.

² The National Assembly of Regional Governments (*Asamblea Nacional de Gobiernos Regionales*, ANGR), the Association of Peruvian Municipalities (*Asociación de Municipalidades del Perú*, AMPE), and the Network of Urban and Rural Municipalities of Peru (*Red de Municipalidades Urbanas y Rurales del Perú*, REMUPRE).

³ See Annex 1 for a full list of interviews

turnover at the subnational level often prevents effective coordination and limits productivity and the continuity of strategies and projects from one administration to the next.

Linking of National, Sectoral, and Regional Strategies – There has been a recent effort to institutionalize the planning process by establishing a chain of planning activities to align national, sectoral, and territorial strategies, and link them to the respective budget. However, although local governments strive to adhere to strategic planning procedures, there is no mechanism to ensure alignment between the various planning instruments.

Availability of Resources – Subnational governments have received greater funding through national programs, and have improved budget execution. Yet, despite the increase in transfers, there remain pressing needs for additional funding for underdeveloped areas with high poverty rates, such as those in Ucayali and Loreto. Some subnational governments have improved own-source revenues, but the development of these types of initiatives are generally constrained by the lack of available human resources.

Public Investment – Although the management of public investment is systematic and project-oriented, some subnational governments still seek to fund their projects outside of the established norms. There have been procedural improvements to make project appraisal and approval more efficient, but new requirements are adding costly delays and creating bottlenecks within the project cycle. As a result, the pressure to identify, evaluate, and prioritize projects is overwhelming the capacity of financial management units and programming and investment offices to control the quality and suitability of many projects. Inadequate supervision of contractors during both the pre-investment and investment stages of the project cycle has resulted in longer project preparation periods, lower quality, and higher costs of implementation.

Transparency and Citizen Oversight – Participatory budgeting is mandated by law, but it is losing influence at provincial and municipal levels. Increased perception of corruption is negatively affecting citizen participation in government as well as public service delivery in Peru. Two critical components of a successful decentralization process, community participation in project identification and project oversight, are weak in most of the locations visited.

Introduction

In the last decade, Peru has been a regional leader in fiscal sustainability, macroeconomic stability, economic growth, and poverty alleviation. Public financial management (PFM) in Peru has been praised by international organizations including the International Monetary Fund (IMF), the World Bank, the Inter-American Development Bank (IADB), USAID, and the Organisation for Economic Co-operation and Development (OECD). Its strong framework and processes received accolades for aligning closely to international practices in the 2009 Public Expenditure and Financial Accountability (PEFA) evaluation. Reviews also highlight the strong alignment of PFM to support fiscal policy outcomes: fiscal discipline, strategic allocation of resources, and efficient delivery of public services.⁴

This report summarizes the findings of an assessment of PFM practices in the two Amazonian regions of Ucayali and Loreto. The first section summarizes the institutional framework of PFM at the subnational level in Peru. The second section describes the current state of PFM in the municipalities visited, highlighting both strengths and challenges of the current system. The report concludes with recommendations for institutional strengthening to help the GoP enhance its capacity to provide public goods and services in a more efficient and effective manner.

Information for this report was obtained through desk research and field work. The purpose of the desk research was to analyze historical, social, economic, and fiscal data on Peruvian municipalities in Ucayali and Loreto and to identify municipalities for further research in the field work phase. Municipalities were selected to ensure geographic coverage and a level of variability in practices. During the field work phase, the PFM-LAC team, comprised of four consultants (including two Peruvian nationals), spent three weeks in May 2014 in Peru. The field work was carried out in Lima, interviewing central government officials and members of subnational government associations, and in the regions of Loreto and Ucayali, interviewing officials from regional, provincial, and municipal governments. Interviews in the regions were also conducted with technical directors from the two regional Planning and Investment Offices (*Oficina de Programación e Inversiones*, OPIs⁵), and public investment specialists from the two regional ConectaMEF⁶ offices. The analysis presented in this report combines information gathered during the interviews, background information provided by donor agencies working in Peru (including USAID/Peru, the World Bank, IADB, GIZ, and SECO), and budget figures from the GoP's integrated financial management system (*Sistema Integrado de Administración Financiera*, SIAF).

⁴ Peru Public Finance Management Report: Based on the Performance Management framework (PEFA). European Union, World Bank, and IADB, 2009.

⁵ OPIs are entities at the national, regional, and municipal level responsible for preparing multiannual public investment plans and providing oversight over SNIP functions. They evaluate and declare project viability for public investment projects. There are more than 920 OPIs around the country, located in every region.

⁶ ConectaMEF offices are the MEF's efforts to extend its presence to the subnational levels. There are 26 offices located in the regional capitals. They provide support, technical assistance, and capacity-building activities on the various public administration systems, including SIAF and SNIP. Personnel in ConectaMEF offices are MEF employees based out of the local area where the office is located.

The team of consultants visited the following subnational governments:



Figure 1: Regions included in study

Region	Municipality ⁷	Population (2011 est.)
Loreto	Belén	67,272
	Loreto (R)	995,355
	Maynas (P)	155,574
	Mazán	12,934
	Punchana	75,124
Ucayali	Campo Verde	13,400
	Coronel Portillo (P)	131,953
	Manantay	70,414
	Nueva Requena	4,966
	Ucayali (R)	471,351
	Yarinacocha	84,372

Table 1: Subnational governments in study

The team prepared a brief questionnaire to capture six qualitative dimensions of PFM at the subnational level as follows:

- **Planning and Budget Preparation:** This dimension evaluates the different types of planning instruments, how information is collected and integrated within municipal and regional plans, budgets and other decision-making mechanisms to allocate resources, and the role of the public authorities in the related processes.
- **Inter-Governmental Coordination:** This dimension evaluates how functions, responsibilities, and resources are distributed, identifies those responsible for each function, and analyzes the effectiveness of this each function in terms of the actual provision of basic public services (e.g., education, health, water and sanitation, etc.).
- **The integration of National, Sectoral, and Regional Plans:** This dimension evaluates the procedures and instruments that help subnational governments align with national and sectoral strategies. This dimension also examines other mechanisms that subnational governments use to access central government funding, and how central government directives influence subnational budget formulation and performance.
- **Availability of Resources:** This dimension examines the availability of funding, or at least the efforts to increase funding, available for public investment.
- **Public Investment:** This dimension examines regional and municipal capacity to identify, evaluate, select, implement, and monitor public investment projects (during the project cycle), and highlights the technical, human, and financial resources that may affect the effectiveness of public investment.
- **Transparency and Citizen Oversight:** This dimension examines citizen participation in the management of public resources. Effective decentralization rests on strong citizen and community participation to monitor and evaluate results, hold public officials accountable, and provide input to adjust the planning and budgeting process to meet the needs of the community.

⁷ “R” denotes regional government; “P” denotes provincial government.

Overview of Subnational PFM in Peru

The system of Public Financial Management (PFM) in Peru includes the institutions, organizations, and systems that regulate and manage public resources within the National Budget. As central, regional, and local (provincial and municipal) governments are all included in the Public Sector Budget, PFM includes these levels of government, with regional and local governments responsible for managing resources, delivering public services, and achieving results. The current state of PFM in regional and local authorities is discussed in the following section, including the impact of ongoing decentralization reforms, the increase in mining royalties (*canon*), and Peru's efforts to modernize the public sector to address PFM challenges. The following discussion provides context for the sections that follow.

1) Despite progress with decentralization reform, many subnational governments still struggle to finance and deliver public services.

Peru has had several waves of decentralization reform. Between 2002 and 2004, the National Congress passed a constitutional reform and several laws that reinvigorated the decentralization process.⁸ A new institutional framework allocated both exclusive and shared responsibilities among the three levels of government. However, despite efforts to establish clear and specific responsibilities, gray zones remained where functions overlapped between regional and local governments, or between all three levels. This was especially true in the design and implementation of sectoral policies. Key features of this wave of decentralization reform were fiscal neutrality and gradualism: responsibilities were to be transferred to subnational governments once sufficient capacity had been verified by the National Government.

Since 2006, the central government has accelerated the transfer of service delivery responsibility to subnational governments, and particularly to regional and municipal governments. According to the Presidency of the Council of Ministers (*Presidencia del Consejo de Ministros*, PCM), as of December 2013, 92.8 percent of the functions assigned to regions had been transferred to the 25 regional governments and the Municipality of Lima, equivalent to 4,466 functions of the 4,810 to be transferred.⁹ Additionally, municipal governments have partially received responsibility for oversight of large social protection programs that were previously administered by the Ministry of Women and Social Development, including the Food Supplement Program (*Programa de Complementación Alimentaria*) and the Nutrition Program (*Programa Integral de Nutrición*).¹⁰ The provision of health services is the responsibility of regional governments and education is the responsibility of municipalities, but there are institutional weaknesses in providing these services.

Unfortunately, decentralization efforts as a whole have not been perceived as effective and remain to be fully implemented. This is mainly due to the lack of complementary financial resources, the weak institutional capacity of subnational governments, and the absence of a normative framework clarifying the distribution of functions by sectors and between the three levels of government. In terms of the provision of critical public services, particularly in education, health, and water and sanitation, the current state is a mix of regional and local government efforts. This lack of clarity affects coordination among

⁸ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013.

⁹ *Informe Anual sobre el Proceso de Descentralización 2013*. Secretaría de Descentralización - PCM, 2014.

¹⁰ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013. See page 33 for exact percentages.

sectors and territories, as well as the interaction between the various levels of government, thus impacting the performance of subnational governments.

The limited progress in decentralization is further magnified by the absence of an instrument outlining the objectives, goals, and required activities to advance reforms, as the National Plan for Decentralization 2012-2016 has not yet been approved. Additionally, the role of the Secretary of Decentralization within the PCM has progressively diminished. The Commission on Decentralization, Regionalization, Local Governments, and Modernization of the State Administration (*Comisión de Descentralización, Regionalización, Gobiernos Locales y Modernización de la Gestión del Estado*) considers it necessary to re-establish the conditions for a new political consensus around the form of government, and the strategy to build it up. The subnational governments support the strengthening of the Intergovernmental Coordination Council (*Consejo de Coordinación Intergubernamental*) within the PCM to promote the establishment of administrative, territorial, and fiscal measures to bolster the decentralization process.¹¹

2) The distribution of financial resources across regions is unequal.

Revenue from mining royalties transferred to subnational governments, especially to municipal governments, has been growing rapidly since 2008. However, these sources of revenue are highly concentrated in a few regions of the country. According to a study by the Multisectoral Commission for Fiscal Decentralization (*Comisión Multisectorial en Materia de Descentralización Fiscal*, CMMDF), the disparity in royalties received by municipalities in 2013 is clear and skewed toward mining-rich regions: S/. 1,557 per capita in Moquegua versus S/. 288 per capita in Ucayali, S/. 128 per capita in Loreto, and S/. 5 per capita in Huánuco.¹² The disparity is only reduced once all other transfers from the central government are included in the analysis, which include revenue from various types of taxes and international donors.¹³

Intergovernmental transfers have been the most important source of financing for the improvement of public services (as opposed to own-source revenues). Municipalities are executing most of their allocated budgets, as is corroborated by this report and by the budget performance indicator of the subnational governments visited (see Annex 3). Improved performance in managing intergovernmental revenue is largely due to the introduction of the National Public Investment System (*Sistema Nacional de Inversión Pública*), or SNIP, and its ability to regulate and organize the identification, evaluation, selection, and implementation of public investment projects at the subnational level. As a result, public investment has been increasing rapidly despite the unequal distribution of resources.

3) The National System for Public Investment is a strong foundation for PFM in Peru.

The SNIP is the Peruvian government's tool for managing public investment projects. The SNIP was established by law in the year 2000, with the underlying tenet that public investment in physical and social infrastructure contributes to economic and social development. The SNIP provides a means to manage the regulations, processes, and actors (including the MEF's Directorate General for Investment Policy, OPIs, and the planning and executing offices of the three levels of government).¹⁴ The SNIP is

¹¹ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013.

¹² *Informe sobre disparidades resultado de la distribución del canon y regalías*. CMMDF, 2013.

¹³ See graph 3 of CMMDF report.

¹⁴ See *Sistema Nacional de Inversión Pública* – available at

http://www.mef.gob.pe/index.php?option=com_content&view=article&id=875&Itemid=100272&lang=es

supported by an information system that has been the vehicle for public investment over the last two decades, and all of the interviewed officials were well-versed with how the system works. The system provides all levels of government with access to the instruments and procedures to identify, assess, prioritize, and evaluate public investment projects which must be aligned with national, regional, and municipal strategies and plans.

The main objectives of the SNIP are to enhance the quality of projects, minimize the waste of public resources, and ensure adherence to national, sectoral, regional, and municipal goals. The current process is comprised of three broad stages designed to achieve the main objectives. A project cycle in the SNIP starts at the pre-investment stage, where a project profile, pre-feasibility assessment, and feasibility assessment must be created and entered into the system (although lower cost projects typically bypass the pre-feasibility assessment). Once the project receives a viability grade, it goes through to the investment stage where a technical study and final assessment are performed, the budget is allocated, and the project execution begins. Finally, in the post-investment stage, resources for operation and management are allocated and the project becomes eligible for ex-post evaluation by an external agency. Figure 2 shows the various stages of the public investment project cycle. In practice, completion of the project cycle depends on the availability of resources, adherence to planning processes, and political will, among other factors.

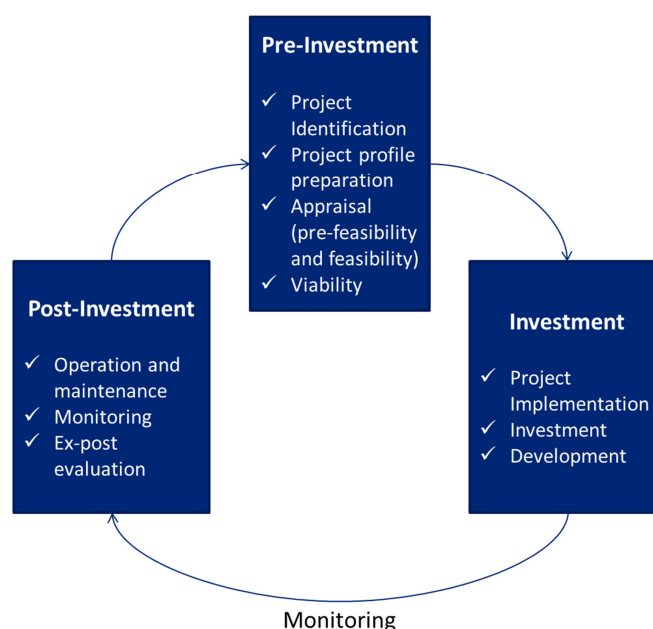


Figure 2: The public investment project cycle

A key feature of the public investment process is the role of the Planning and Investment Offices (*Oficinas de Programación e Inversiones*, OPIs) administrative entities within subnational governments and ministries. OPIs act as the gatekeepers, evaluating project profiles developed by planning offices (*unidades formuladoras*) during the pre-investment stage. The SNIP contains the guidelines, methodologies, and technical requirements for project identification and the profile preparation process, and the OPI oversees the qualification and approval of a project during the different stages (acting like checkpoints). Finally, SNIP procedures require that all projects be kept in the “Bank of Projects” until they are formally included in the budget during the investment stage. Budgetary entities at every level of

government must use the SNIP for their public investment projects in order to receive their budget allocations. The typical pre-investment procedure is as follows:

1. Planning office (*unidad formuladora*) develops the project profile and registers the profile in the Bank of Projects. The system automatically assigns an OPI for the profile evaluation.
2. Assigned OPI receives the project profile, validates registration in the Bank of Projects, and evaluates the profile using the approved protocol.
3. OPI prepares a technical report and submits it in the Bank of Projects. Depending on the characteristics of the project, this report will be used to:
 - a. Approve the profile and authorize the development of the next study (pre-feasibility/ feasibility);
 - b. Submit the viability report;
 - c. Provide observations that will need to be addressed by reformulating the profile; or
 - d. Reject the project.

Previously, the MEF would certify the quality and sustainability of public investment projects, but these tasks are now carried out by ministries and local and regional officials. The MEF's Directorate General of Investment Policy still maintains the ability to intervene at any time, though this generally only occurs if a project is of national significance, or if critical financial management problems might affect the implementation of the project at any level of government. It should also be noted that despite the current design, in practice, the project cycle is often prolonged, or even disrupted, when there is insufficient funding (due to factors such as poor profile preparation and improperly forecasted costs), when projects remain uncompleted for long periods, or when governments do not effectively monitor project execution.

4) *Public investment has increased, supported by a strong PFM framework.*

Over the last ten years, the economy of Peru has sustained a 6.5 percent annual average growth rate, poverty levels have decreased from 54 percent to 25.8 percent, and the unemployment rate has declined to record lows of approximately 4 percent.¹⁵ These are outstanding results even by international standards. During this same period, public investment increased from 2.8 percent of GDP to 5.6 percent of GDP, while private investment jumped from 15 percent of GDP to over 20 percent of GDP; most of the latter went into mining, while the former went into productive infrastructure and the provision of public goods and services.¹⁶

Most striking during this period of abundant growth is the change in public expenditure and investment percentages by level of government. Between 2004 and 2013, total central government spending declined from 72 percent to 67 percent, while its share of public investment decreased from 52 percent to 32 percent. Simultaneously, the share of total spending by subnational governments increased from 28 percent to 33 percent while their share of public investment increased from 48 percent to 68 percent. In absolute values, central government investment increased from S/. 2,733m to S/. 9,860m, while public investment by subnational governments rose from S/. 2,553m to S/. 21,451m. In other words, while central government public investment only grew threefold, subnational governments' public investment increased nearly tenfold.¹⁷

¹⁵ World Bank Databank. This figure does not include numbers for those who participate only in the informal economy.

¹⁶ Staff Report for the 2013 Article IV Consultation – Peru. IMF, January 24, 2014.

¹⁷ See Annex 3, Tables 1 and 2

PFM in the regions of Ucayali and Loreto

This section highlights the current state of PFM in Ucayali and Loreto. Information is drawn from interviews of administrators in the regions of Ucayali and Loreto, as well as officials from the MEF.

Planning and Budget Preparation

1) Subnational governments use tools such as SIAP and national budget programs (Programas Presupuestales) to guide processes and strategic planning decisions, but there is weak alignment between planning and budgeting.

The national planning system in Peru is undergoing a transitional period due to institutional changes set by legislative decree no. 1088, approved in 2008. Until 2005, the sectoral planning process was led by the Vice-Minister of Economy (VME) and its main instrument was the Multiyear Sectoral Strategic Plan (*Plan Estratégico Sectorial Multianual*, PESEM). At the subnational level, planning was guided by the Joint Regional Development Plan (*Plan Regional de Desarrollo Concertado*, PRDC). Decree no. 1088 created a planning body, the National Center for Strategic Planning (*Centro Nacional de Planeamiento Estratégico*, CEPLAN), assigned with overseeing the national system of strategic planning. Previously, there was no framework to coordinate national, regional, and local development plans, which largely explained the limited coverage of national planning. With resolution no. 26-2014-CEPLAN/PCD, approved in April 2014, the GoP introduced the normative framework to organize and align planning across the three levels of government, which is currently in the process of implementation. The national government has experienced difficulties implementing these changes. Since its creation, CEPLAN has played a limited role in the planning process, and only very recently has begun to more actively promote planning.

Budgets must be prepared and approved annually in Peru as mandated in the Constitution. However, MEF's Director of the National Budget explained that the GoP has implemented multiannual planning. Additionally, to strengthen the link between strategies, plans, and budgets at all levels, the GoP introduced Budgeting for Results (BfR) in 2007, and has been gradually expanding the scope of the BfR framework. The purpose of BfR is to match budget allocation with prioritized results. It emphasizes the targeting and measuring of results with the collection of data, which is analyzed against strategic targets and benchmarks and monitored by entities via specific indicators. Traditional budgeting practices focus on inputs, financial regularity, and adherence to legal procedures, while BfR permits greater flexibility of inputs and process, and places a greater emphasis on results (see Figure 3).

BfR will link allocations to results by:

- i. Extending BfR to subnational governments;
- ii. Gradually increasing the number and coverage of national programs to cover the majority of planned expenditures;
- iii. Using performance information to promote more efficient and effective allocation of resources;
- iv. Creating an accountability culture that provides feedback for ex-post adjustments;
- v. Implementing multiannual expenditure planning;
- vi. Improving the linkage between current and capital expenditures; and
- vii. Strengthening territorial coordination.

Figure 3: Linking allocations to results¹⁸

¹⁸ Marco Macroeconómico Multianual 2013-2015. MEF, May 2012.

The subnational governments visited prepare their own annual budgets and other documents in accordance with the National Budget Law. Under the current planning process, the MEF notifies entities regarding budget ceilings within the first five working days of June. Budget directives and circulars must be reviewed by the subnational governments, and the MEF provides a schedule for budget meetings to negotiate draft budgets in accordance with the budget ceilings. Regional and municipal budgets, which are prepared using the SIAF-GL¹⁹ module, are approved at the central level. The full budget draft is then submitted to the National Congress for approval by August 30.

In general, the team observed that most municipalities visited have well-functioning budget preparation processes and that officials receive regular training and support from ConectaMEF offices. Yet, budgets are not always approved by the MEF and may not be used to inform national policy, despite the fact that they are being prepared. Meanwhile, the GoP intends to use BfR as a national tool to improve the quality of public expenditure. The government plans to link budget allocations to results through strategic national budget programs.

All of the officials from the municipalities visited were aware of the MEF's plan to fully adopt the BfR framework beginning in FY 2015. The officials currently seek funds through established national programs, and as such, claim to be prepared to transition to the BfR framework. However, based on the limited availability of trained human resources at the subnational level, it is highly likely that most subnational governments will require assistance to fully adopt BfR. The MEF's directive for implementing BfR provides the normative framework for all government levels.²⁰ All public entities must comply with this directive, but a key issue for further investigation is to determine how entities (both line ministries and subnational governments) are actually complying with the process given their current capacities and constraints.

The weak linkage between policy, planning, and budgeting may be the most important factor contributing to poor budgeting outcomes at the local level. The team observed that policy making, planning, and budgeting take place independently of each other, suggesting that the planning systems of the three levels of government are still fragmented. By law, regional and municipal governments should periodically prepare their respective Development Plans (*Planes de Desarrollo Concertado*, PDC); however, this formal exercise has become disconnected from the budget preparation process. Planning at the subnational levels is instead often confined to the planning of investment activities, mainly identifying, selecting, and implementing public projects that align with existing national programs. Overall, this has led to a mismatch between what is promised through government policies and what is actually achieved. The annual budgeting process, therefore, has become more about attending immediate needs, rather than allocating resources on the basis of clear policy objectives.

¹⁹ The SIAF is the official system for recording, processing and generating information related to public sector's financial administration. Local governments use a customized module adapted for subnational governments, called SIAF-GL. See http://www.mef.gob.pe/index.php?option=com_content&view=article&id=2028&Itemid=101421&lang=es.

²⁰ *Directiva No. 001-2013-EF/50.01: Directiva para los programas presupuestales en el marco de la programación y formulación del presupuesto del sector público para el año fiscal 2014*. Available at http://apps5.mineco.gob.pe/resulta/pdf/Directiva_001_2013EF5001_Programas_Presupuestales_2014.pdf

Inter-Governmental Coordination

2) *Current law does not clearly specify the service delivery related functions of each administrative level of government.*

Although the composition of the administration of each level of government is well-defined in the law, the functional responsibility of each level, as well as the role of each level in the provision of basic public services, are not specifically defined. In many cases, authority over delivery of services is shared between the MEF, the sector ministry or respective regional sector office, and – to a lesser extent – the local government. The explicit definition of sectoral responsibilities and roles between levels of government is still a work in progress and one of the main impediments to effective decentralization.

The Regional President is the highest political and administrative authority at the regional level, while a Regional Council exercises supervisory authority. The Regional Government develops and implements the Regional Development Plan (*Plan Anual de Desarrollo Regional Concertado*) and the Regional Participatory Budget (*Presupuesto Regional Participativo*), while the Regional Council approves both and oversees their execution. There is a Regional Coordinating Council, an advisory

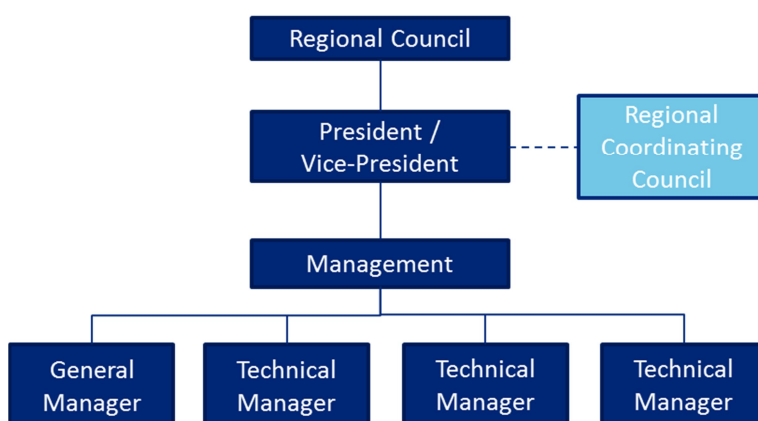


Figure 4: Regional administrative structure

body that coordinates with municipalities, comprised of the Provincial Mayors and representatives from civil society organizations. The Regional General Manager is an administrative officer responsible for the management of the regional government. Planning and Budget Managers are in charge of programming, executing, and controlling the regional budget through the SIAF to ensure the smooth execution of the budget. The Regional General Manager and the regional technical managers (e.g., Planning and Budget, Economic Development, Social Development, Infrastructure, and Natural Resources and Environment) are appointed by the Regional President.

Similar to the organization at the regional level (see Figure 4), at the local level, the Mayor is the highest authority in a municipality (both provincial and district) and is usually a politician supported by an administrative body similar to that of regional governments. Municipalities are required to develop a Municipal Development Plan (*Plan de Desarrollo Concertado Municipal*) as well as a Participatory Budget. A Local Council approves and supervises both the Plan and the Participatory Budget. The structures of all municipal administrations are relatively similar, and only differ in sectoral components and staff size, which vary according to population and financial resources.

The described administrative structure does not define how coordination should take place between the various levels of government. In fact, interviewees described instances of how coordination can break down and negatively affect service delivery. Administrators from the regional government of Loreto explained that substantial responsibility for health and education functions was transferred to their government within the past two years, but that effective service delivery did not follow. The officials

mentioned that there was poor coordination between the various ministries and agencies responsible for health outcomes. Even where there was overlap in the objectives of budget programs managed by these different central level entities, there was no administrative or financial synchronization, or coordination between the different levels of government. Each central level entity maintained its own requirements and desired outcomes without accounting for how they would affect lower levels of government or whether subnational governments would be able to meet these requirements. In the education sector, the administrators from the different levels of government (Ministry of Education, regional government, and provincial governments) were not able to reach an arrangement concerning administrative oversight and, as a result, no indicators were selected for the 2014 fiscal year. Government officials were then unable to give clear direction to teachers and education administrators regarding educational objectives.

3) While most subnational officials are competent and well-trained, high personnel turnover is negatively impacting the quality of public service delivery.

The larger governments serving more densely populated regions receive proportionally more funding, and are more likely to employ better qualified professionals, and offer better compensations, than the smaller subnational governments. Several interviewees, particularly from the MEF, cited i) low productivity and ii) poor qualifications as two of the main reasons for the low quality of public service delivery. The high-level officials interviewed at the subnational governments visited suggested a different explanation for the low quality of public service delivery. They indicated that the high turnover of public employees limits productivity and continuity, as well as prevents effective coordination with other governments, but that otherwise most regional governments and municipalities were staffed with competent and well-trained employees.

The general and sectoral managers interviewed were mostly technical practitioners (e.g., economists, accountants, teachers, and lawyers) with extensive experience in the public sector. The general managers in the municipalities visited were highly knowledgeable of the strategic planning and budgeting processes. Most of the sectoral managers interviewed were also well-trained with relevant experience. With the exception of a few individuals in the smallest municipalities, the majority of the officials interviewed demonstrated a clear understanding of their role and responsibilities. Directors of the Planning and Budget offices and the officials responsible for OPI offices (in both Loreto and Ucayali) deserve special mention. All interviewed were dedicated individuals that conveyed strong command of the roles and processes, including the respective information systems. Similarly, the two directors of the ConectaMEF offices (in both Loreto and Ucayali) seemed to be very knowledgeable and dedicated.

The high incidence of personnel turnover and rotation described by the senior officials was observed in the field interviews. Representatives from technical offices provided examples of how the high employee turnover negatively affected productivity. Technical staff in OPIs explained that they often took on administrative tasks outside of their job descriptions to maintain continuity after the departure of clerical staff. Even with the contracting out of some technical tasks, the officials in the two OPIs visited claimed that, due to the increase in the number of projects to be appraised, they spent most of their time attending to bids to contract out the preparation of the project proposals, reviewing documents presented for appraisal and viability, and monitoring the advances of projects during the investment stage. Therefore, they did not have time to dedicate to preparing terms of reference for project formulation, exercising adequate quality control over appraisal documents before they were sent to the central government for final approval, or replying to the many inquiries from the central government about ongoing financial and

economic analyses in a timely manner. In other words, they had to spend a large portion of their time ensuring that administrative duties were completed, which prevented them from focusing on technical tasks.

Linking of National, Sectoral, and Regional Strategies

4) *Local governments strive to adhere to strategic planning procedures, but there is no mechanism to ensure alignment between the various planning instruments.*

There has been a recent effort to institutionalize the planning process in Peru by establishing a chain of planning activities to ensure the link between the national strategy, sectoral and territorial strategies, and the respective budget (see Figure 5).²¹ According to regulations, local governments' development plans (*Planes de Desarrollo Local Concertado*, PDC-GL) must include the strategies to achieve the government goals as established in the PEDN, the PESEM (in relation to the shared responsibilities), and the Regional Government Development Plan (*Plan de Desarrollo Regional Concertado*, PDC-GR). Additionally, according to the law, development plan goals must be reflected in the institutional strategic plan (*Plan Estratégico Institucional*, PEI), the institutional operational plan (*Plan Operativo Institucional*, POI), and the institutional budget (*presupuesto*). In theory, by nesting all the plans, tying them to budgeting and expenditure, and maintaining a national system for public investment, prioritized projects should contribute to advancing the national objectives of closing socio-economic gaps and increasing economic competitiveness.



Figure 5: The strategic planning chain for territories²²

Contrary to expectations, just a few of the local governments visited have developed new PDCs. Most incoming governments update the versions left by previous administrations, as officials from Maynas, Nueva Requena, and Yarinacocha explained. None of the officials interviewed have shared and discussed in depth the content of their development or operational plans with the public. Some officials admitted to the lack of utility placed on development plans. Officials from the municipality of Belén, for example, explained that their current plans (development, strategic, and operative), were developed for short horizons and did not cross-reference one another or even the national, regional, or provincial development plans.

Although the CEPLAN directive was approved in the first semester of 2014, three methodological guides that should have been included have yet not been finalized. This lack of guidance affects how plans should be developed and updated, the quality of the content, and how they should be implemented, and

²¹ General directive for the planning process of the National System for Strategic Planning (*Sistema Nacional De Planeamiento Estratégico*). Presidential resolution to the council no. 26-2014-CEPLAN/PCD. Directive no. 001-2014-CEPLAN. CEPLAN. *Centro Nacional de Planeamiento Estratégico. El Peruano. Diario Oficial*. April 6, 2014.

²² Resolution no. 26-2014-CEPLAN/PCD, Directive no. 001-2014-CEPLAN. CEPLAN. *Centro Nacional de Planeamiento Estratégico. El Peruano. Diario Oficial*. April 6, 2014.

raises questions regarding the continuity of plans. It was clear that every municipality visited maintained or has prepared development, strategic, and operational plans as required by the new law. However, even with a directive to align national, sectoral, and regional policies, there appeared to be poor linkage between the various development plans, likely stemming from the apparent lack of priority given to developing the plans by administrators. According to interviewees, there is also little continuity in the implementation of approved plans and projects following the arrival of a newly-elected administration. All of the officials interviewed admitted that when their government came into power, little attention was given to continuing the previous administration's policies.

Availability of Resources

5) Subnational governments have experienced increases in resources from national programs while improving overall budget execution.

Transfers to subnational governments from mining royalties (*canon* and *regalías*)²³ have been growing rapidly since 2008. However, the country's natural resources are highly concentrated in a few regions and local jurisdictions, and these are the sole recipients of these funds. According to a study by the CMMDF, the disparity in royalties received by regions in 2013 was significant: S/. 1,557 per capita in Moquegua, versus S/. 288 per capita in Ucayali, S/. 128 per capita in Loreto, and S/. 5 per capita in Huánuco.²⁴

A growing portion of non-*canon* funds are being allocated to national programs (created by MEF and central level ministries). Budget figures show that larger percentages of resources for municipalities are coming from “*recursos ordinarios*” (General Fund).²⁵ Additionally, MEF has introduced an incentive fund²⁶ to advance public administration reforms at the municipal level; municipalities that meet certain criteria and goals are awarded additional funds on top of approved allocations. According to SIAF figures, local governments sought funding through 32 national programs totaling S/. 5,865m in 2013. All of the subnational governments visited largely accept and work within the scope of the MEF's programs, as they help finance local projects, help subnational governments meet established goals, and help municipalities qualify for additional financing through the incentive fund. There were four national programs of particular importance to public officials in all municipalities visited, focusing on child malnutrition, education, citizen security, and water and sanitation. Officials interviewed indicated that they worked hard to reach program goals, as well as to create projects that were complementary and within program scope. The municipalities were particularly interested in meeting results in these programs in order to collect the incentives from the fund that ties performance to additional disbursements. In Mazán and Maynas, officials mentioned that their child nutrition projects were of particular importance to the communities, not only for provision of services but also for the incentive funding associated with achieving national program goals.

²³ *Canon* refers to funds collected by the central government from rents for the exploitation of natural resources (e.g., mining, natural gas, fishing, etc.) which are transferred to subnational governments in those same zones. *Regalías mineras* are royalties that the national government receives from concessions for the mining of nonrenewable resources. *Regalías* are justified as compensation for national resources before their depletion.

²⁴ *Informe sobre disparidades resultado de la distribución del canon y regalías*. CMMDF, 2013.

²⁵ *Recursos ordinarios* refers to revenues from certain taxes and fees, but which are not earmarked. The percentage of total funds transferred through “*recursos ordinarios*” was 17.6% in 2009, 18.9% in 2011, and 23.8% in 2013 according to SIAF figures.

²⁶ *Plan de Incentivos a la Mejora de la Gestión y Modernización Municipal*. Details available at http://www.mef.gob.pe/index.php?option=com_content&view=article&id=2221&Itemid=101547&lang=es.

Regardless of funding source, public investment by subnational governments has been increasing rapidly, from S/. 2,553m in 2004 to S/. 21,451m in 2013. Meanwhile, public investment from the central government increased from S/. 2,733m to S/. 9,860m during the same period. In percentage terms, public investment by subnational governments was 48 percent of total public investment in 2004 and 68 percent in 2013. The increase in budget resources and public investment has also been followed by improved budget execution over the past few years. Loreto and Ucayali showed regional budget execution rates²⁷ of 91 percent and 92 percent respectively in 2013. The average for their municipalities was around 85 percent and 79 percent for provinces.²⁸ Efforts to improve budget management have been confirmed by the high budget execution rates in municipalities with the four national programs promoted by the MEF.

6) *Many subnational governments are improving own-source revenue²⁹ mobilization.*

Officials in the municipalities visited are becoming increasingly aware of the maintenance and operational costs associated with public investment projects. These costs have typically not been included in the budget at project inception. Officials are often forced to cover these costs with funds from outside of the approved project budget, such as funds from the entity's operational budget. Some officials mentioned cases of abandoned facilities, because the municipality or regional government did not have the resources to pay for personnel or maintenance costs, as was the case in Mazán, Punchana, and the regional governments of Loreto and Ucayali. This has caused officials to be more conscientious of improving project costing and to seek out other sustainable ways to cover these recurring expenditures.

As a means to protect projects from funding shortfalls, some municipalities have begun property rights legalization initiatives that will enable the municipality to create a cadaster and increase collection of local property taxes. Coronel Portillo, for example, has already allocated 4,000 home titles to citizens living in informal housing settlements and expects to reach close to 20,000 titles within the next four years. Manantay is also implementing a similar property rights program. The municipality of Mazán has been utilizing SIAF-Rentas, a module of SIAF developed by MEF, to help improve property tax collection rates in the community. Even officials from the small municipalities of Belén and Punchana discussed their desire to organize property rights legislation, though neither municipality possesses the financial resources or human capacity to implement these activities.

Other municipalities facing budget shortfalls have found it necessary to start charging fees to help defray the costs of public services, such as water and sewage systems, garbage disposal, and open-air market facilities. Subnational governments have come to realize that the one of the most effective ways to expand coverage and improve the quality of services is by charging for a portion of the cost and by exerting close oversight over service provision with the help of the community and beneficiaries. As such, there is now an urgency to establish or strengthen service units to manage and finance those services. In Mazán, the community and municipal authorities reached an agreement to pay for the gasoline needed to produce energy and pump water for a water purification system. The municipality of Belén and the provincial

²⁷ Budget execution is the process by which the financial resources made available to a public sector entity are directed toward achieving the purposes and objects for which budgets were approved. The process involves compliance with both legal and administrative requirements.

²⁸ All figures from SIAF.

²⁹ "Own-source revenue" refers to the revenue that a subnational government raises by levying taxes, collecting user fees, or by generating business and other income. If subnational governments have no control over the base and rate of a tax, it is not a subnational source of own-source revenue. Transfers from the central government, for example, are not own-source revenue.

government of Coronel Portillo are developing plans to organize and formalize the use of land that is currently being informally used for open markets in their respective communities. Vendors will be expected to pay modest rents or fees for using the space. While this is still in the planning stages in Belén (the government is still seeking funds to implement the project), officials from the provincial government of Coronel Portillo have already begun investing in the construction of the market using own-source revenues.

Public Investment

7) The management of public investment is systematic and project-oriented, but many subnational governments still perceive the need to seek financing outside of established procedures.

Every official interviewed was familiar with all aspects of the SNIP and its relevant information systems. In some of the municipalities visited, officials have sought additional training to improve their technical knowledge of project preparation, in particular of pre-investment studies, costing, and other technical aspects. Employees from the regional government of Ucayali, and the municipalities of Manantay and Yarinacocha, confirmed that they have received training or attended workshops developed by national government entities on these topics. Officials from the provincial government of Maynas have also received capacity training, and provided the most comprehensive description of how they manage their Bank of Projects, as well as the tools used for project management (including the SIAF module “Infobras”). Officials from the smaller municipalities, including Belén, Mazán, Punchana, and Campo Verde, explained that they generally received direct assistance from sectoral ministries when they needed to develop very technical projects where their own staff’s knowledge was limited.

The SNIP provides the tools for smaller municipalities to plan and implement projects that help address important socio-economic gaps. For example, the municipalities of Campo Verde, Yarinacocha, Mazán, and Maynas have all successfully received funds to finance different types of projects for housing, urban infrastructure, and water sanitation systems. However, during interviews, officials revealed that their administrations can also resort to methods outside the established system to seek funding for projects. Regional and municipal governments often present project proposals directly to line ministries in Lima with the hope that a well-developed project will be considered for financing through the respective sector’s or entity’s own budget. Even the President of the Republic is asked to evaluate and consider financing projects presented by mayors and regional presidents during visits to the regions. Although verbal acceptance by a sector entity or political actor does not ensure financing, petitioners are aware that a sound project proposal could win approval and potential inclusion in the National Budget.

8) SNIP procedures have mostly increased the efficiency of project appraisal and approval.

The well-established culture of project-oriented public investment, institutionalized through the SNIP, helps to explain the positive absorption of resources transferred to subnational governments arising from the mining boom. Instead of directing resources to subnational governments through budget allocations, the MEF uses national programs, which align to national development objectives, to silo public investment into prioritized strategic areas. Subnational governments receive their annual budget allocations, which are used for operations and limited public investment. Resources not directly transferred to subnational governments or earmarked to national programs become part of either MEF or a sectoral ministry budget. Subnational governments bid for additional funds from competitive funds (*fondos concursables*) by developing technical proposals for strategic public investment projects that

align with the sector's objectives. In other words, subnational governments compete for funds beyond their annual allocations, and the way to win additional funding is by developing plans for public investment projects that are attractive to the central government.

Due to the increasing number of projects financed by resources from the mining boom, the MEF's then-Directorate for Multiannual Programming³⁰ (*Dirección General de Programación Multianual*, DGPM) transferred project evaluation responsibilities to line ministries and regional and local governments in June 2006 (Law 28802). In 2007, the DGPM approved the regulations of the SNIP. Since this time, subnational governments have been able to contract out the development of project proposals and feasibility studies (pre-investment stage), while OPIs retain responsibility for conducting project appraisals and provide technical approval. Contracting out has helped subnational governments to improve budget execution, as they have been able to identify, prepare, and receive approval for more projects, keeping pace with the resource increases, and raising the expectations of their communities in the process.

Despite these procedural improvements, requirements such as the Environmental Certification (*certificación ambiental*) are creating bottlenecks in the project cycle. In theory, these certifications, which are granted by the Ministry of the Environment, are intended to ensure that public investment projects do not have adverse effects on the environment. According to interviewed officials, however, these certifications are becoming a substantial cost to a project proposal. Officials described the certification process as an additional step in the pre-investment stage that requires the subnational government initiating a project proposal to physically deliver the required documentation and environmental studies to the Ministry in Lima. Depending on the type of study required, both the preparation and the approval can take several weeks, with additional time and trips to Lima required if the studies are incomplete or rejected.³¹

9) Bottlenecks at the pre-investment stage are causing costly delays in the project cycle.

Although public investment's capacity to generate growth should not be taken for granted, deficiencies in public investment appear to arise from poor selection and implementation of projects, weak technical expertise in identifying, preparing, and managing complex projects, and the lack of information for monitoring and evaluation. Public investment in a weak institutional environment runs the risk of undermining potential benefits, becoming instead an obstacle to fiscal sustainability and economic and social development. Accordingly, there are bottlenecks along the project cycle affecting the quality, efficiency, and effectiveness of public investment.

Despite advances, such as contracting out the development of project proposals during the pre-investment stage, there are increasing complaints from the central government about the quality of the appraisals of many projects, generating higher costs and creating delays during the investment stage. During the interviews, the team identified difficulties with respect to i) the workload burden making it difficult for OPI officials to carry out their responsibilities adequately, ii) the excessive amount of time taken in the

³⁰ Now called the Directorate General for Public Investment (DGIP)

³¹ See Ministry of the Environment's presentation on the Environmental Impact Evaluation System, available at http://www.google.com.pe/url?sa=t&rct=j&q=&esrc=s&frm=1&source=web&cd=12&ved=0CFMQFjAL&url=http%3A%2F%2Fsiar.regionlalibertad.gob.pe%2FadmDocumento.php%3Faccion%3Dbajar%26docadjunto%3D1452&ei=tD09VNGdBsr5yOTN0IHgDA&usg=AFQjCNEZo1EC9rKn_Qv3IurGuku0gb2qpQ.

development of project proposals, and iii) the large number of contradictions and inconsistencies between project proposals and appraisals for approval (i.e., the financial/economic analysis is not adequate). Except for Manantay, officials from the remaining governments all expressed these types of challenges. The regional government of Ucayali cited an example of a hospital project that took six years to complete, where preparing the project profile to eventually win approval took three years.

Regional and local governments in Ucayali and Loreto have been able to identify, prepare, and implement a large number of projects that meet SNIP requirements. However, the costs of executing these projects, in terms of time and quality, have become substantively high. Projects with high rates of economic and social return are given insufficient attention, while others of arguably dubious benefits, low quality, and posing higher risks, are rushed through the system because these plans are easier to prepare and often less technically demanding. To address these types of problems, the GoP is carrying out (with the help of the IADB) an ambitious program to strengthen the capacity of regional and local governments to identify, evaluate, and prioritize projects with high social and economic impact.³² The goal is to provide public officials in financial management units and OPIs with the capacity to perform their duties as established in SNIP norms and regulations. Efforts to increase technical capacity of officials during the pre-investment stages can trickle down to the subsequent stages, and make the public investment project cycle a more efficient process overall.

Transparency and Citizen Oversight

10) Participatory budgeting is mandated, but it is losing effectiveness at provincial and municipal levels.

According to the Law of the Participatory Budget, the provincial municipalities and civil society organizations are required to participate in the prioritization of public expenditure. Many municipalities utilize participatory budgeting to guide planning and to prioritize projects based on citizen feedback. In the provincial government of Maynas and the municipality of Punchana, officials described the general timeframes and formats of the participatory budget town halls, and provided percentages or amounts of budget funds allocated to projects selected during these meetings. The government of Maynas was the most open and detailed about their use of participatory budgeting. They explained the use of town hall meetings open to all citizens and civil society groups exclusively for participatory budgeting. According to interviewed officials, between 14 to 15 percent of the province's budget was assigned to projects selected during participative budget meetings. This figure was further divided for distribution between municipalities within the province and funds for the province (approximately S/. 3.8m and S/. 4.7m in 2014, respectively).

In the majority of municipalities visited, however, community participation in budgeting appears to be decreasing. According to interviewed officials, many citizens were weary of long sessions that do not lead to actionable items. Additionally, many discussions are growing more technical in complexity, discouraging further participation as most citizens are often unprepared to interpret such information. According to some reports, community involvement in participatory budgeting activities has increased

³² *Hacia un Modelo de Asistencia Técnica a Gobiernos Regionales en Gestión de Inversión Pública: Sistematización de Experiencias. Secretaría del Consejo de Ministros. Secretaría de Descentralización. MEF, Dirección General de Programas Multianuales, 2011.*

mostly in regions receiving substantial *canon* transfers, while it has decreased in regions with average or decreasing financial resources.³³ In Loreto, community participation has almost disappeared, while in Ucayali, participation decreased rapidly over a recent period, but has improved in the last two years.

11) Increased perception of corruption is negatively affecting citizen participation in government as well as public service delivery in Peru.

The increase in public investment that resulted from the mining boom has yielded more projects and better execution of budgets in many subnational governments, but it has also unequivocally increased the opportunities for corruption. Peru is now the largest cocaine producer in the world, and illegal mining and logging have proliferated.³⁴

Allegations of corruption and indictments at the subnational level have increased in recent years.³⁵ Many subnational governments in the two regions visited have been facing challenges with mayors who are under investigation or have been removed from office. The interviewed mayors from Campo Verde, Yarinacocha, and the regional government of Loreto were either newly appointed after the prior mayor had been removed, or were investigating corruption allegations at the time of the team's field visit.

There is little effort by the National Government's auditors or civil society to hold local governments accountable. According to several analyses, the increase in financial resources has not only been improperly controlled, but transparency in budget execution has also diminished.³⁶ The press regularly reports on the allegations of corruption, but there is noticeable absence of civil society organizations ready and willing to advocate on behalf of citizens and demand greater accountability from elected officials.

³³ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013.

³⁴ "Divide and bribe: Corruption and political fragmentation threaten Peru's democracy." *The Economist*. 11 October 2014. Available at <http://www.economist.com/news/americas/21623706-corruption-and-political-fragmentation-threaten-perus-democracy-divide-and-bribe>.

³⁵ *Diecinueve presidentes de gobiernos regionales deben responder por 158 casos de corrupción*, *La Republica*, 28 May 2014. Available at <http://www.larepublica.pe/28-05-2014/19-presidentes-de-gobiernos-regionales-deben-responder-por-158-casos-de-corrupcion>.

³⁶ Open Budget Index scores for Peru have decreased from 66% to 65% to 57% in the years 2008, 2010, and 2012 respectively. See <http://internationalbudget.org/what-we-do/open-budget-survey/country-info/?country=pe>.

Opportunities for Strengthening PFM in the regions of Ucayali and Loreto

This section highlights opportunities for improving PFM. Each subsection draws attention to the most significant challenges that the team identified within a given dimension, and provides examples of interventions that may be undertaken by the GoP in partnership with the bilateral and multilateral development organizations.

Planning and Budget Preparation

1) Assist subnational governments to develop program-based budgets that align to national programs and sectoral strategies, while taking into consideration local priorities.

The MEF's national programs and system of incentives are playing a prominent role in how subnational governments plan and prepare their budgets. Under the current system, subnational governments coordinate less with sectoral ministries while favoring the aspects of the budget which fall within national priorities. Many of the officials interviewed emphasized results from national programs in education and water sanitation, but did not always mention their interactions with the Education, Housing, or Environmental Ministries in order to achieve the best possible outcomes. Additionally, CEPLAN is not actively involved with subnational governments. From the interviews, it became apparent that MEF is seen as the driver of both planning and budgeting. For example, officials from the Regional Government of Ucayali explained that they recently worked with MEF directly on examining their strategic investment portfolio, but that CEPLAN has not provided assistance to subnational governments with planning. In Coronel Portillo, officials explained that they see MEF as influencing public expenditure, because they provide additional financial incentives when municipalities meet the objectives of selected national budget programs.

Although national programs help to focus public investment, some officials described challenges with aligning goals within annual budgets due to the timing constraints of the national budget process. For instance, in Coronel Portillo, the officials explained that the budget must be prepared at the end of the current fiscal year, but that the goals and indicators for many national budget programs are disseminated once the new fiscal year begins. As a result, officials must anticipate the goals and indicators for the coming year, further demonstrating the fragmentation between planning and budgeting.

Possible areas for intervention:

- Assist subnational governments to respond to the MEF circulars and related instructions, including training to build awareness of national objectives, programs, and the indicators which will be used to measure results.
- Assist subnational governments to develop programs that align to national sectoral strategies and to develop actionable activities based on an analysis of local needs and prior year performance.
- Assist subnational governments to provide budget development guidance in order to disseminate information to other levels of government, as well as neighboring municipalities.

2) Assist the MEF to systematize the development of performance indicators across the whole of government to improve monitoring and evaluation and strengthen planning.

The implementation and adoption of BfR at the subnational level, using national programs, requires further investigation. After visiting Loreto and Ucayali, it became apparent that there are a handful of national programs that are working well, as funds are distributed to subnational governments and these governments execute these funds, but a more comprehensive evaluation of the gaps to corroborate the feasibility of implementing BfR at the subnational level is still needed.

There are two concerns that may affect how programs are developed and managed as BfR is institutionalized at all levels of government in Peru. In a basic BfR model that aims to improve the efficiency and effectiveness of public expenditure by linking the funding of activities to the results they deliver, there are two fundamental requirements: i) the ability to create programs that connect sectors and subnational governments through specific activities with clearly defined outputs, impacts, and indicators; and ii) the availability of information about the objectives and results of government expenditure. Key performance indicators and simple program evaluations are necessary for decision-making authorities to enhance, adjust, or dismiss activities and assign responsibilities for the results obtained. Neither of these two requirements is yet in place in at the subnational level. While it was apparent from the interviews that local governments implement national budget programs and collect information on specific budget programs indicators, there appears to be no systematic data collection methodology and no clarity concerning which entities are responsible for data collection. Subnational governments are aware of the connection between performance indicators and the budget implications, but data collection, monitoring, and evaluation will need to be strengthened.

Implementing BfR will require a robust system of data collection at the subnational level to allow for systematic performance management. Regional governments will play a critical role in the BfR process, as sectors and line ministries cannot reach 1,836 municipalities directly—they need intermediate actors to coordinate the evaluation of national programs. In this regard, the efforts of the MEF and PCM to establish a unified monitoring and evaluation system to monitor prioritized policy results should be mentioned, as such a system would supply decision-makers in the Presidency, the PCM, CEPLAN, and the MEF with the information to evaluate and steer strategic government programs and projects.

Possible areas for intervention:

- Provide assistance to MEF in its efforts to implement a unified monitoring and evaluation system that will allow authorities to control and monitor projects in line with strategic objectives.
- Assist MEF with identifying mechanisms to improve the selection and relevance of performance indicators for the diverse regions and sectors.

Inter-Governmental Coordination

3) Assist local officials to collaborate with representatives from line ministries to refine and strengthen local service delivery.

The pace of decentralization reform in Peru has slowed considerably. After tremendous advances in transferring responsibilities to subnational governments, subnational governments still struggle to finance and effectively manage local service delivery in certain sectors. The subnational governments have expressed their opinion on the need for the PCM to promote the establishment of administrative,

territorial, and fiscal measures to strengthen the decentralization process. The President himself agrees with the need to open a political dialogue on enhancing the decentralization process and improving the provision of public services.³⁷

The unclear definition of roles and responsibilities between levels of government has delayed effective decentralization. In the health and education sectors, for example, there are no clearly defined or accepted service delivery standards for clinics and schools. There are no established procedures for the hiring of staff in these entities, which affects quality control, the collection of relevant performance information, and ultimately the monitoring and evaluation of public services. These circumstances have negatively affected service delivery as well as the regional government's ability to qualify for funds that are disbursed only if the government can meet goals and indicators established by the different central government entities.

In the municipalities visited, it was clear that the fragmented coordination between different levels of government over service delivery and partisan politics greatly influenced how municipalities receive funds from the regional governments. There were cases where municipalities coordinated with provincial or regional governments only because they were working on a previously approved shared project rather than because there are defined methods for inter-governmental coordination. Some interviewed officials mentioned that their municipality was excluded from receiving funds from the regional or provincial government because their administration was not from the same political affiliation as the regional or provincial government.

Possible areas for intervention:

- Partner with service delivery providers to help them identify bottlenecks in decentralizing service delivery; assist in the development of standards and mechanisms that guide service delivery quality at the subnational level while improving coordination between national level actors and subnational service delivery providers.
 - Identify special cases (municipalities with high need/low capacity) to pilot targeted social assistance programs led by central government entities (e.g., sectoral ministries).
 - Assist sector ministries to establish standards and measures that localities may use when creating programs.
- 4) *Assist subnational governments during political transitions (pre and post elections) by providing training and guidance to help both prospective and new officials assume roles and maintain continuity.***

According to the officials interviewed, particularly from smaller municipalities such as Mazán, Campo Verde, and Nueva Requena, both administrative and technical personnel often leave within a few months of their hire date for various reasons. Meanwhile, the learning curve for new hires can be high, especially for technical personnel charged with managing the identification and preparation of public investment projects, which is among the most complex of responsibilities. The public investment specialist from the ConectaMEF Pucallpa office in Ucayali, explained that MEF used to provide training and capacity building workshops to local governments, but given the high turnover rates (i.e., trained staff would no

³⁷ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013.

longer be in the same position 3 to 4 months later), the MEF subsequently curtailed ConectaMEF's capacity-building activities.

In addition to high personnel turnover within single administrations, several officials highlighted additional challenges that emerge during an election year when there is a change in administration. At the time of the interviews, there were no systematic or standardized procedures to transfer responsibilities to incoming administrations; instead, the handover was an informal exercise. As a result, officials noted, the first few months in office were often wasted hunting down required information on existing plans and projects, confirming upcoming deadlines, and even searching for where information is stored. This has come to the attention of the central government, and in June 2014, a law regulating these transfers at the subnational level (law no. 30204). The Office of the Comptroller has not yet approved the official guidance on administrative hand-overs as of October 2014.

Even with the official directive, subnational governments would benefit from assistance to help ensure continuity in the provision of public services. Only the officials from the provincial municipality of Maynas described what their transfer process would entail after the elections in October, and how they have organized their "Bank of Projects" (with prioritized projects and progress reports for those being implemented) to hand over to the new administration. Officials from both regional governments particularly underscored the importance of transfer of responsibilities and their desire for additional assistance. Although the USAID-funded project *ProDescentralización* (ProDes) has piloted activities around post-election transfers of power in selected municipalities in Loreto, San Martin, and Ucayali, this is an area where supplementary efforts may benefit additional governments and improve public administration overall.

Possible areas for intervention:

- Develop transfer of responsibilities, checklists, and relevant guidance to assist new administrations to maintain continuity over public service delivery improvement and public investment projects already in execution.
- Assist the National Civil Service Authority (SERVIR) with the creation and delivery of capacity-building workshops to public employees. Provide training and technical guidance on recordkeeping and financial management procedures, particularly as it pertains to public investment and the Bank of Projects.

Linking of National, Sectoral, and Regional Strategies

5) Assist local officials to coordinate with national planning offices in the preparation of local development plans that align with national objectives.

Development Plans should be formulated for eight-year horizons, but only a few of the local governments visited developed new PDCs or updated the existing plans. Despite CEPLAN's directive to align national, sectoral, and regional policies, there appears to be poor linkage between the various development plans at the different levels of government visited. There is also little continuity in the implementation of approved plans and projects from an outgoing administration by a newly elected administration. Officials from Belén, Punchana, and the regional government of Ucayali corroborated their administrations' need to attend to campaign platforms, even if they were in opposition to the previous administrations' activities.

As mentioned in the previous section, the principal method for achieving national and subnational governments' objectives is through public investment and by developing projects that aim to achieve the strategic goals as established in national budget programs. Many of the projects proposed to the communities by the officials from the municipalities visited seem to originate from campaign promises and more immediate pressing demands rather than from the established planning process. However, there can be disparities between what is promised and what is actually achieved, since those priorities may not match those of the national government.

Possible areas for intervention:

- Assist local officials to host strategic planning workshops with CEPLAN/MEF through ConectaMEF offices.
- Assist subnational governments to map goals and relevant operational activities to national plans. Provide guidance on dissemination so that these documents are available to regional and provincial governments, as well as neighboring municipalities to promote cooperation.

Availability of Resources

6) Assist municipalities with efforts to increase financing for relevant public investment projects through the established mechanisms, such as national programs and own-source revenues.

Although there have been increases in overall transfers from the central government to subnational governments, according to all of the interviewed officials from subnational governments and representatives from the subnational government associations,³⁸ these increases have not been commensurate with the new responsibilities transferred to the subnational governments. There remain pressing needs that require additional funding in underdeveloped areas with high poverty rates, such as those in Ucayali and Loreto. Intergovernmental transfers have been an effective way to increase financial resources for a locality, but the process requires close coordination between all levels of government.³⁹ Instead, regional and municipal governments have found it productive to prepare project proposals and present them directly to the corresponding ministry or agency in Lima, bypassing SNIP procedures. Public investment decisions based on political considerations at the central level introduce inefficiencies in the project preparation cycle and may actually contribute delays in financing for other critically needed public infrastructure or service delivery enhancement projects.

In this context, many municipalities have increased efforts to collect own-source revenues from property taxes and fees for public services to make up for budget shortfalls. A small municipality like Mazán, for example, has been using a SIAF-GL module, SIAF-Rentas, to manage and track property tax collection. While the municipality still struggles with high delinquency rates, the tool has allowed them to better monitor payments. The use of the tool has had spillover effects, as the officials have also been able to improve payment rates for electricity and water services. According to interviewees, delinquency rates for electricity payments dropped from nearly 100% 5 years ago, to around 25% in 2014. In Coronel Portillo, there is a large public area used for an informal open-air market that had been costly for the city in terms of clean-up expenses, the provision of water, and illegal delivery of electricity. Instead of closing the

³⁸ AMPE, REMURPE, and ANGR

³⁹ In some cases the value of the project is shown in the budget of the financing entity but not in the budget of the receiving entity.

space, the government came to an agreement with the vendors to formalize the market. While only government invested in the construction, now that it is finished, the vendors are charged fees to use the space and defray maintenance and operations costs.

Such efforts, led by the subnational governments, provide examples of initiatives that could be piloted in other areas in order to increase revenues. Although nearly every official expressed interest in improving own-source revenues, these types of initiatives tend to fall beyond their capacity, as they do not have the staff, technical knowledge, or surplus funds to implement such schemes.

Possible areas for intervention:

- Assist subnational governments with efforts to improve own-source revenue mobilization (e.g., land property rights initiatives, fee-for-service arrangements, etc.) through the creation of pilots to demonstrate feasibility while strengthening municipal capacity to promote the activity and provide oversight.

Public Investment

7) Provide assistance to subnational governments to improve the management of the public investment cycle, particularly during the pre-investment phase.

According to interviewees, a project's cycle, from conception to final approval, may last up to two years. In some cases, depending on project cost,⁴⁰ it could be as much as three years, as was the case with a hospital project mentioned by the regional government of Ucayali. During this time, the cost of the hospital increased from S/. 120m to S/. 420m due to deficiencies with the project profile and appraisal documents that led to project approval. Additionally, during construction, many technical issues that were not properly identified in the appraisal (particularly the economic analysis) caused delays. Problems with building and staffing standards (which are not consistent between Lima and Ucayali) also led to unanticipated cost overruns.

During the pre-investment stage, there is a considerable amount of time spent in consultations between private sector contractors and the OPIs, clarifying and resolving inconsistencies between the terms of reference for a project profile and the technical document that the contractors prepare. Most of these inconsistencies arise because the two sides often make different assumptions in the project profile between the pre-investment and investment stages, contractors do not spend sufficient time or effort in developing the project profile, or there is simply poor quality control at both ends. It was mentioned that contractors frustrated with the process often walk away from a contract, as the fines are so low that they prefer to take a financial loss than complete the deliverable.

During the pre-investment appraisal process, prices and standards are the most commonly mentioned causes of disagreements and disputes between subnational governments and the central government approvers. For example, in Ucayali and Loreto, transportation costs are a substantive component of total project costs and are much higher than in other parts of the country. Officials in the two regional governments and some municipal governments explained that Lima rejected many of their cost estimates in project appraisals, particularly as they related to transportation costs. When the officials in Lima

⁴⁰ Approval processes are different for projects of higher value (i.e., above S/.10 million)

compared similar projects between regions, those in Ucayali and Loreto always seemed too costly, leading to skepticism about their costing and additional time-consuming demands for explanations. This extended the project cycle further.

Longer project cycles are also related to issues of continuity between different administrations. Local governments are elected for only four years, so when a project's cycle lasts longer than four years for any number of reasons, a single administration is not able to see the project through to completion. Because a new administration generally focuses on its own priorities first, projects started or approved by the previous administration, which should enter the investment stage, no longer take precedence. Officials from Campo Verde explained that they faced problems with implementing projects that were approved by the previous administration, claiming that they did not have adequate funding for the execution of said projects with the annual budget that was subsequently approved.

Possible areas for intervention:

- Develop checklists that describe standards for project creation and establish clear criteria for project evaluation.
- Provide technical assistance at the municipal level in project management fundamentals in order to deepen the institutional capability of municipal oversight functions in the project planning and execution cycle.
- Provide training to OPI technical staff in project appraisal and the capacity to link proposed projects with the multi-annual planning framework being introduced by the GoP. Assist the National Civil Service Authority (SERVIR) with the creation and delivery of capacity-building workshops to both technical staff and private sector contractors.
- Provide technical assistance to public investment evaluators at all levels of government on financial and economic analysis. Appraisals should include rigorous financial and social cost-benefit analyses before a project is deemed viable and receives final approval.

8) *Strengthen or improve existing procurement regulation so that it is responsive to the needs of subnational governments.*

The procurement of civil works and technical services is one of the biggest challenges in the project cycle. In Peru, as in many other Latin American countries, legislators do not give sufficient consideration to the impact that overly restrictive procurement laws, which come into effect during the investment stage, have on budget execution. Difficulties with the present procurement law have caused such a high degree of resentment that the national government sent a new law to the Congress for consideration, and it was approved in July 2014. The regulations and implementing directives have not yet been approved as of October 2014.

With respect to awarding contracts to implement approved projects, subnational governments in Ucayali and Loreto prefer non-competitive contracting. The reasons vary, from lack of available qualified contractors in these regions, to legal difficulties that arise over the selection of winning proposals in competitive bidding. It is quite common for entities to get involved in lengthy legal challenges over the designation of a winner, as the procurement law allows contractors to dispute a government's award in a competitive bid and paralyze the investment process. Officials from Manantay, for example, mentioned a dispute with contractors over the award of a child nutrition project in which the losing bidders appealed

the decision and prevented the government from going forward with the project, forcing instead a new selection process.

To minimize work with contractors, most of the local governments visited have their own construction machinery for certain types of public works. Even a small municipality like Nueva Requena is acquiring machinery to produce materials for constructing roads in a strategic transportation project, thereby avoiding transactions with contractors, and at the same time looking for ways to earning money to finance other projects.

Possible areas for intervention:

- Assist subnational governments with the implementation of the new procurement regulations.

Transparency and Citizen Oversight

9) Review existing community oversight mechanisms and organizations currently part of the participatory process and assist MEF to revise or develop new mechanisms to enable civil society to effectively advocate for greater transparency and promote citizen oversight.

Participatory budgeting has been in effect for several years, and this has been more recently expanded to participatory planning. However, community participation in planning and budgeting appears to be waning. Weak citizen participation was noted by interviewees in Belén, Punchana, Nueva Requena, and Campo Verde. Nueva Requena has a diverse population that includes various native communities, but according to officials, they do not actively engage with or integrate into the community or its politics.

Involvement in the participatory budget has increased mostly in regions with large *canon* transfers, while it has decreased in regions with average resources.⁴¹ For Ucayali and Loreto, this means that two critical components of a successful decentralization process, community participation in both project identification and project delivery oversight, are losing influence.

Possible areas for intervention:

- Conduct a survey of civil society organizations to develop an inventory of successful participatory practices at the subnational level in coordination with Secretary for Public Management and the MEF in order to inform the development of a modernization law.

⁴¹ *Informe anual sobre el proceso de descentralización: los retos de la gestión descentralizada*. ProDes (USAID/Peru), 2013.

Summary of Opportunities to Strengthen PFM

PFM Dimension	Observation	Interventions or Assistance
Planning and Budget Preparation	Subnational governments are increasingly relying on national budget programs to finance social development projects, often at the expense of local priorities.	<ul style="list-style-type: none"> Assist subnational governments to respond to the MEF circulars and related instructions, including training, to build awareness of national objectives, programs, the indicators which will be used to measure results. Assist subnational governments to develop programs that align to national sectoral strategies, and to develop actionable activities based on an analysis of local needs and prior year performance. Assist subnational governments to provide budget development guidance and to disseminate information to other levels of government as well as neighboring municipalities.
	Implementing BfR will require a robust system of data collection at the subnational level to allow for systematic performance management.	<ul style="list-style-type: none"> Provide assistance to MEF in its efforts to implement a unified monitoring and evaluation system that will allow authorities to control and monitor projects in line with strategic objectives. Assist MEF with identifying mechanisms to improve the selection and relevance of performance indicators for the diverse regions and sectors.
Inter-Governmental Coordination	Politicization of decentralization reform has slowed progress in further clarifying the division of responsibilities between regional, provincial, and municipal governments in service provision, affecting the quality of public services.	<ul style="list-style-type: none"> Partner with service delivery providers to help them identify bottlenecks in decentralizing service delivery; assist in the development of standards and mechanisms that guide service delivery quality at the subnational level while improving coordination between national level actors and subnational service delivery providers. Identify special cases (municipalities with high need/low capacity) to pilot targeted social assistance programs led by central government entities (e.g., sectoral ministries). Assist sector ministries to establish standards and measures that localities may use when creating programs.

PFM Dimension	Observation	Interventions or Assistance
	High personnel turnover and post-election transitions negatively affect public service delivery at the subnational levels.	<ul style="list-style-type: none"> • Develop transfer of responsibilities, checklists, and relevant guidance to assist new administrations to maintain continuity over public service delivery improvement and public investment projects already in execution. • Assist the National Civil Service Authority (SERVIR) with the creation and delivery of capacity-building workshops to public employees. Provide training and technical guidance on recordkeeping and financial management procedures, particularly as it pertains to public investment and the Bank of Projects.
Linking of National, Sectoral, and Regional Strategies	Development and operational plans are underused in municipalities, undermining the purpose of the central government's strategic planning process.	<ul style="list-style-type: none"> • Assist municipalities to host strategic planning workshops with CEPLAN and MEF through ConectaMEF offices. • Assist subnational governments to map goals and relevant operational activities to national plans. Provide guidance on dissemination so that these documents are available to regional and provincial governments, as well as neighboring municipalities to promote cooperation.
Availability of Resources	Subnational budgets are insufficient to meet increasing responsibility for public service delivery.	<ul style="list-style-type: none"> • Assist subnational governments with efforts to improve own-source revenue mobilization (e.g., land property rights initiatives, fee-for-service arrangements, etc.) through the creation of pilots to demonstrate feasibility while strengthening municipal capacity to promote the activity and provide oversight.
Public Investment	Longer project cycles, arising from various types of bottlenecks, result in cost overruns and delays in delivering public services.	<ul style="list-style-type: none"> • Develop checklists that describe standards for project creation and establish clear criteria for project evaluation. • Provide technical assistance at the municipal level in project management fundamentals in order to deepen the institutional capability of municipal oversight functions in the project planning and execution cycle. • Provide training to OPI technical staff in project appraisal and the capacity to link proposed projects with the multi-annual planning framework being introduced by the GoP. Assist the National Civil Service Authority (SERVIR) with the creation and delivery of capacity-building workshops to both technical staff and private sector contractors.

PFM Dimension	Observation	Interventions or Assistance
		<ul style="list-style-type: none"> Provide technical assistance to public investment evaluators at all levels of government on financial and economic analysis. Appraisals should include rigorous financial and social cost-benefit analyses before a project is deemed viable and receives final approval.
	Existing procurement laws are not designed to promote efficiency in public investment.	<ul style="list-style-type: none"> Assist subnational governments with the implementation of the new procurement regulations.
Transparency and Citizen Oversight	Participatory budgeting is losing influence in the subnational planning process.	<ul style="list-style-type: none"> Conduct a survey of civil society organizations to develop an inventory of successful participatory practices at the subnational level in coordination with Secretary for Public Management and the MEF in order to inform the development of a modernization law.

Annex 1: Interviewed Officials

Date	Entity	Meeting	Position
LIMA			
12 May	USAID/Peru	Cara Thanassi	D&G Director
		Sobeida Gonzales	Project Mangement Specialist
		Beverly Busa	Budget and Financial Management
		Victor Llajaruna	Financial Analyst
		Gregory Swarin	Deputy Office Chief, Project Development and Programs
13 May	MEF	Rodolfo Acuña	Dirección General de Presupuesto Público; Calidad de Gasto Presupuesto por Resultados
		Cristina Mendoza	Dirección General de Presupuesto Público; Calidad de Gasto Presupuesto por Resultados
		Carlos Ricse	SIAF II
		Juan Pichihua	Dirección General de Descentralización Fiscal y Asuntos Sociales
		Raquel Yamujar	Dirección General de Descentralización Fiscal y Asuntos Sociales
		Alex Carbajal	Dirección General de Descentralización Fiscal y Asuntos Sociales
		César Liendo	Dirección General de Política Macroeconómica
		Laura Calderón	Coordinadora, Grupo de Estudio de Programa de Mejoramiento Continuo de las Finanzas Publicas
		José Valderrama	Grupo de Estudio PMCFP
		Carlos Oliva	Vice Ministro de Hacienda
14 May	REMURPE	Carlos Arana	Coordinador
	REMURPE	Carlos Lopez	Coordinador
	World Bank	Karina Olivas	Peru Country Officer
	GIZ	Mayra Ugarte	GIZ
	SECO	Binolia Porcel	SECO
	Banco Central	Luis Alberto Arias	Banco Central
15 May	ANGR	Eduardo Ballon	Secretario Técnico
	AMPE	Ivan Vega	Coordinador
	AMPE	Eduardo Carhuaricra	Gerente
	ProDes	Violeta Bermudez	Jefe de Proyecto, PRODES (TetraTech ARD)
16 May	MEF	Eloy Durand Jesus Ruiton	Presupuesto de Inversiones – Inversión Publica, Política de Inversiones
	MEF	Carlos Calderon Henry Espinoza	DGPP – Calidad de Gasto
	MEF	Samuel Torres	DGPP – Director de Articulación de Presupuesto Territorial
	GIZ	Mayra Ugarte	GIZ
	Technical Expert	Donny Chumpitaz	Experto, Gobiernos Subnacionales
UCAYALI			
19 May	Yarinacocha (M)	Abog. Boris Pinedo Alonzo	Gerente Municipal

Date	Entity	Meeting	Position
		Sixto Ramos	Gerente de Planeamiento y Presupuesto
		Sameico ¿?	Contador
	Campo Verde (M)	Sr. Maximiliano Supa Carhuas	Alcalde
		Sr. Marcos Pérez	Gerente Municipal
		Eco. Marco Mori Vásquez	Gerente de Planeamiento y Presupuesto
	Coronel Portillo (P)	Sr. Segundo Pérez Collazos	Alcalde
		Hugo Tuesta Saldaña	Gerente Municipal
		Eco. Miguel Valdivieso	Gerente de Planeamiento, presupuesto y racionalización
20 May	Ucayali (R)	Arq. Ricardo Mejía	Gerente General del GRU
		Eco. Jorge Ruíz	Gerente de planeamiento, presupuesto y acondicionamiento territorial
		Ing. Lutgardo Gutiérrez Valverde	Gerente de Desarrollo Social del GRU
		Ing. Antonio López Ucariegue	Gerente de Desarrollo Económico
		Ing. Franz Tang	Gerente de RR.NN. y GMA del GRU
	Manantay (M)	Ing. Guillermo Chino Mori	Alcalde
		Ing. Patricia Gonzáles	Gerente Municipal
		Eco. Rolando Palacios	Gerente de Planeamiento, presupuesto y racionalización
21 May	Nueva Requena (M)	Sr. Humberto Banda Estela	Alcalde
		Sr. Carlos Ayllón	Gerente Municipal
		Ing. Guillermo Tello	Gerente de Infraestructura
	ConectaMEF Ucayali, Pucallpa	José Verde	Especialista de Inversión Pública
LORETO			
23 May	Belén (M)	Ing. Hermógenes Flores	Alcalde
		Ing. Ames Rodríguez	Gerente Municipal
		Econ. Edward Díaz	Gerente de Planificación y Presupuesto
		Sr. Rommel Flores	Gerente de Desarrollo Social y Económico
		CPC Gladys Arnedo	Administrador
	Loreto (R)	Lic. Iván Vásquez	Presidente Regional
		CPC Roberto García	Gerente General Regional
		Dr. Yuri Alegre	Gerente Regional de Desarrollo Social
		Dr. Hugo Rodríguez	Director Regional de Salud
		Econ. Fernando Cárdenas	Gerente Regional de Planeamiento Presupuesto y Acondicionamiento Territorial
		Abog. Lira Reátegui	Gerente Regional de Recaudaciones
		CPC Fernando Lazo	Jefe de la Oficina Regional de Administración
	Punchana (M)	Lic. Juan Cardama	Alcalde

Date	Entity	Meeting	Position
26 May		Abog. César Cabezas	Gerente Municipal
		CPC Cristian Chirito	Gerente de Planificación y Presupuesto
		Lic. Alex Antezana	Gerente de Desarrollo Social y Económico
		CPC Paul Navarro	Administrador
	Maynas (P)	Arq. Adela Jiménez	Alcaldesa
		Abog. Víctor López	Gerente Municipal
		Econ. Carlos Pezo	Gerente de Planificación y Presupuesto
		Ing. Ericka Eriquiño	Gerente de Desarrollo Social
		Dr. Jaime Fartolino	Gerencia de Promoción Económica
		Econ. Marco Mesía	Administrador
	ConectaMEF Loreto, Iquitos	Francisco Javier Cardenas	Especialista de Inversión Pública
	Mazán (M)	Odont. Edward Reátegui	Alcalde
		Econ. César Zumaeta del Castillo	Gerente de Planificación y Presupuesto
		Lic. Educ. Dardo Ayambo	Gerente de Desarrollo Social y Económico
		Lic. Adm. Pedro Ampuero	Administrador

Annex 2: Detailed Observations by Locality

Strategy, Planning, and Budgeting		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Planning and budgeting considers projects, social needs, operational needs Have the ability to substantiate requested budget increases to central government 	<ul style="list-style-type: none"> Mentioned that budgeting is difficult because they generally do not have sufficient funds to cover operations or projects under newly-transferred functions (particularly in health and education) Some planning includes agreements with municipalities, but this is especially difficult in the Loreto region given the size and isolation of many communities
Maynas (P)	<ul style="list-style-type: none"> Budget is planned from projected revenues 14-15% assigned to projects selected during participative budgeting 	<ul style="list-style-type: none"> Issues with continuity – mentioned that incoming administrations generally have no interest in continuing previous administration's agenda (development plans, strategic projects, etc.) Need to improve the transfer process from one administration to the next – currently there is no systematized plan or set of procedures Officials mentioned that strategies and assigned budgets do not adequately reflect the unique needs of the jungle region of Peru
Belen	<ul style="list-style-type: none"> Planning is very focused on the needs of the community – but leads to problems with aligning with national plans because the priorities do not always match 	<ul style="list-style-type: none"> Special case – very poor community, social gaps higher than average Budgets generally have to align with budget programs to solicit needed funds – objectives from these programs do not always match municipality's priorities Planning not done on multiannual basis – short-term planning is the norm in the operating offices
Mazán	<ul style="list-style-type: none"> Planning and budgeting takes into account national priorities Use participatory budgets 	<ul style="list-style-type: none"> Budgeting issues include reallocation of funds for operations to investment/projects Have not been strategic about targeting budget programs in order to compensate for shortfalls in investment budget
Punchana	<ul style="list-style-type: none"> Budgeting considers both operational needs and most important social gaps to address 	<ul style="list-style-type: none"> Challenges with trying to plan and budget for some social projects – need to be included in Operational Plan to be allowed, doesn't always occur
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> Focusing planning around sustainable development rather than single projects Have worked with MEF on a strategic investment portfolio – planning on a multiannual framework, learning how to prioritize projects 	<ul style="list-style-type: none"> Mentioned the noticeable absence of CEPLAN in planning function Mentioned that regions are not solicited in policy-making at central level for certain functions including environment and education They face problem with planning for and

Strategy, Planning, and Budgeting		
Municipality	Strengths	Development Areas
		<p>administering in areas where they have limited background or skills</p> <ul style="list-style-type: none"> • Believe that some multiannual horizons are not realistic (e.g., development plan to extend to 2050)
Coronel Portillo (P)	<ul style="list-style-type: none"> • Use participatory budgeting, have raised citizen expectations in planning, budgeting, and prioritizing projects 	<ul style="list-style-type: none"> • Budget composition has changed – lower allocation for operations and investment from central transfers; they must rely more on requests from budget programs and sectoral ministries • Co-financing several large projects since 2011 (water sanitation, potable water, road construction); central government funds 50%, but officials say this is not sufficient • Link between planning and budgeting is complicated by timing, because the national strategic goals are published in January of fiscal year, but the budget is prepared the previous year; that is, when budget is prepared, they do not have information about the goals or strategies
Campo Verde	<ul style="list-style-type: none"> • Funds from budget programs make up a large portion of budget; continuously seek funds from additional sources outside of budget • Manual system for goals has helped them monitor indicators and reach goals in various budget programs • Can plan and budget with relative certainty about transfers from the central government 	<ul style="list-style-type: none"> • Special case – very poor community, social gaps higher than average • Need assistance with project prioritization – 2013 budget passed without strong vetting of many projects (proper technical criteria) • Budget programs mostly do not address some of the community's most critical needs • Multiannual planning has been a difficult adjustment – many projects were approved in previous years that cannot be completed
Manantay	<ul style="list-style-type: none"> • One of the newest municipalities (about seven years old), but also the most organized of the sample group • Local planning takes into account development goals, strategic plan • As of 2014, everything will be implemented within BfR framework 	<ul style="list-style-type: none"> • Face some difficulties with budgeting for certain types of operational costs because they do not fit well within BfR framework
Nueva Requena	<ul style="list-style-type: none"> • Planning and budgeting all done at municipal level • Relative certainty about operating and investment budget, though government is indebted 	<ul style="list-style-type: none"> • Special case – very poor community, social gaps higher than average • Generally are not able to plan projects with central government, as many of their projects would not pass environmental requirements/checks
Yarinacocha	<ul style="list-style-type: none"> • Aware of new requirements for planning and budgeting (BfR, multiannual budgeting) • National priorities and budget programs have been helpful in improving some indicators (but not sufficient) • Use multiannual plans to guide operations, budgeting 	<ul style="list-style-type: none"> • High personnel rotation, problems with continuity • Difficult to plan projects with municipalities, region, provinces – coordination is weak, often hindered by political differences

Inter-Governmental Coordination		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Coordinate directly with many central level sectoral ministries 	<ul style="list-style-type: none"> Intra-governmental coordination is weak (19 executing units), need to modernize structure of regional government Some planning includes agreements with municipalities, but this is especially difficult in the Loreto region given the size and isolation of many communities
Maynas (P)	<ul style="list-style-type: none"> MEF recently provided assistance – how to align development plans, how to prioritize projects, how to improve participative budget Strategic investment plans shared with other provinces 	<ul style="list-style-type: none"> Strategic investment plans not used or closely monitored
Belen	<ul style="list-style-type: none"> Strong relationship with central level (sectoral ministries) Receive most assistance from central government Receive a lot of media attention due to special circumstances (social gaps among the highest in Peru) 	<ul style="list-style-type: none"> Do not have strong relationship with regional government (political differences)
Mazán	<ul style="list-style-type: none"> Working with three other municipalities on building a landfill for the communities Working directly with various central level sectoral ministries 	<ul style="list-style-type: none"> ConectaMEF not doing a good job of reaching their municipality – they are farther from Iquitos than many other communities
Punchana	<ul style="list-style-type: none"> Co-financing project with regional government Maintain relationship with central level ministries (education, housing) 	<ul style="list-style-type: none"> Do not have strong relationship with provincial government (political differences)
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> Have worked directly with MEF on a strategic investment portfolio 	<ul style="list-style-type: none"> Mentioned need to clarify role of each government within shared functions (particularly health and education) Do not have a strong relationship with many central level sectoral ministries Mentioned that they should be more involved with municipalities, participate in more projects with their governments
Coronel Portillo (P)	<ul style="list-style-type: none"> Coordinate with some municipal governments on various types of projects Work with Health ministry, have reduced child malnutrition in the province Water and wastewater project example of coordination: Planning by regional government, co-financed by sectoral ministry and province, administration by municipalities 	<ul style="list-style-type: none"> Mentioned poor coordination with central level and regional level Have not received funds from regional governments in the last four years Mentioned at least three sectoral ministries that are noticeably absent in the regions: Housing, Environment, Transportation Acknowledged that they should work closely with more municipal governments
Campo Verde	<ul style="list-style-type: none"> Working on project with regional government (water sanitation) 	<ul style="list-style-type: none"> Organic structure of municipal government too rigid, not properly adapting to service delivery on the most important social issues Weak coordination with provincial

Inter-Governmental Coordination		
Municipality	Strengths	Development Areas
		<p>government (have not received financial assistance in at least two years)</p> <ul style="list-style-type: none"> Coordination with regional government is not strong
Manantay	<ul style="list-style-type: none"> Working with sectoral ministry (Housing) to set up cadaster Working with MEF 	<ul style="list-style-type: none"> Problems with monitoring and reporting of indicators – generally, monitoring is done by sectoral ministries and their methodology is not always clear, or ministries' figures do not match internal figures kept by municipal government
Nueva Requena	<ul style="list-style-type: none"> Receive funds from provincial government, central government (Housing ministry, DEVIDA [Peru's Development Agency]) 	<ul style="list-style-type: none"> Coordination is ad hoc No response yet from regional government on funds request
Yarinacocha	<ul style="list-style-type: none"> Good relationship with regional government (have implemented road construction projects) Good relationship with some sectoral ministries 	<ul style="list-style-type: none"> Officials find that collaboration with other municipal governments is not easy Mentioned political differences as an obstacle to collaboration

Linking of National, Sectoral, and Regional Policies		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Government worked with the seven provinces to create linked regional policies Working with many local governments to link local development plans to regional goals 	<ul style="list-style-type: none"> Face very unique regional problems that the central level entities in Lima do not consider Still do not reach all municipalities given the size of the region and the difficulty in physically accessing many communities
Maynas (P)	<ul style="list-style-type: none"> Plans align to national and sectoral policies Recently approved new development plan (2014-2021) 	<ul style="list-style-type: none"> Although plans are linked to regional priorities, they have actually been affected by reduction in budget, as many responsibilities have been transferred to regional governments Strategic investment plans not used or closely monitored Although development plan should be updated on an annual basis, in reality this is not done
Belen	<ul style="list-style-type: none"> Government has development, operating plans, but these are not updated Generally base their development plans and approved projects on what they ran during election campaigns 	<ul style="list-style-type: none"> Plans not well articulated with national or regional development plans – national priorities do not align with the community's most pressing needs
Mazán	<ul style="list-style-type: none"> Working within national priorities in the following areas: education, health, child malnutrition, housing, women's health (pregnant and nursing mothers) Working with six other municipalities to reduce illegal logging 	<ul style="list-style-type: none"> National policies to meet certain goals in health are beyond their capacity – very dispersed community that is not easy to access, many citizens do not have IDs and cannot be registered in national systems Did not explicitly discuss their development plans or whether they are guiding documents for the administration
Punchana	<ul style="list-style-type: none"> Plans are linked to national and sectoral policies 	<ul style="list-style-type: none"> Coordinating some projects with regional government, but do not have closely aligned

Linking of National, Sectoral, and Regional Policies		
Municipality	Strengths	Development Areas
	<ul style="list-style-type: none"> Align municipal goals to national objectives through budget programs (Pension 65, Beca 18, Una Mas, Juntos, SIAN, and others) Have met 100% of goals in program budgets since last year 	objectives (except for road construction)
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> Plans are linked to national policies (CEPLAN directives) Operative plans include multiannual portfolio of strategic projects Focus of plans is to reduce many social gaps (as directed by national policies) 	<ul style="list-style-type: none"> Do not believe that regional governments are sufficiently involved or solicited when central government is setting sectoral policies or priorities Find it hard to meet specific outcomes that central government has elaborated without consulting regional governments (example given in education was number of books that must be distributed to students)
Coronel Portillo (P)	<ul style="list-style-type: none"> Use participatory budget to link development plans and prioritize projects in the province to regional and national policies Several projects currently under execution align to national policies (MEF) because they are financed through budget programs 	<ul style="list-style-type: none"> Currently in investment stage of a project that does not align to national priorities, but a priority for the province (open air market) Linking of priorities with actual budget is complicated, because the goals are published in January of fiscal year, but the budget is prepared the previous year; when budget is prepared, they do not have information about the goals or strategies
Campo Verde	<ul style="list-style-type: none"> Plans align to sectoral policies 	<ul style="list-style-type: none"> Deloitte team quickly reviewed development and operational plans – appeared to be too general to be guiding documents
Manantay	<ul style="list-style-type: none"> Most organized municipality Plans are aligned to annual expenditure (operating, strategic, development, vision) All plans are multiannual 	<ul style="list-style-type: none"> Planning offices for three managing areas (public works, public services, social development) ensure that projects align to national and sectoral policies
Nueva Requena	<ul style="list-style-type: none"> Many of the national and sectoral priorities coincide, attempting to meet these objectives (esp. child malnutrition, education outcomes, citizen security) 	<ul style="list-style-type: none"> Social gaps exceed what has been prioritized by central government Local economic development objectives do not coincide with central government priorities (e.g., want to expand palm oil extraction to create jobs, but this would not be supported by central government because it does not meet environmental goals)
Yarinacocha	<ul style="list-style-type: none"> Elaborate own development plans, try to align to PEDN 	<ul style="list-style-type: none"> Plans are very general and do not provide strategic guidance Although there are some mechanisms to encourage collaboration with other subnational governments in terms of planning and approving projects, political differences often prevent cooperation and strategic alignment of plans

Availability of Resources		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Have requested and successfully been awarded some funds under central level budget programs – but these are not a large portion of their investment budget 	<ul style="list-style-type: none"> Do not feel prepared to take on recently transferred responsibilities because these are not followed by commensurate increases to their budgets Do not receive budget funds for operations from central government because they receive funds from <i>canon</i>
Maynas (P)	<ul style="list-style-type: none"> Have requested and successfully been awarded funds under central level budget programs and from sectoral ministries (Housing, MIDIS) Bottlenecks in SIAF are minimal, mainly related to previous year's debts 	<ul style="list-style-type: none"> Budget funds have been reducing (mainly from <i>canon</i> and <i>sobrecanon</i>⁴², the Municipal Compensation Fund [FONCOMUN]) End use of certain budget funds too restrictive – Officials feel that these restrictions do not take into account the special circumstances that the jungle region faces
Belen	<ul style="list-style-type: none"> Receive funds from central government transfers including <i>canon</i>, budget programs, sectoral ministries' budgets 	<ul style="list-style-type: none"> Do not receive assistance from central government entities in their efforts to improve own-source revenue Community does not want to contribute to improving services by paying fees or taxes – requires a culture change Because it is a very small community and transfers are determined by population without considering social or geographic factors, they feel that they never receive sufficient funds
Mazán	<ul style="list-style-type: none"> Some improvements in collecting fees for services, but still a very small fraction of total revenue Have utilized SIAF-Rentas to improve tax collection rates 	<ul style="list-style-type: none"> Financing some operations with investment funds rather than operational funds Have not been strategic about requesting funds from some budget programs to increase their budget
Punchana	<ul style="list-style-type: none"> Receive funds from transfers, <i>canon</i> Successfully received funds from sectoral ministries (Education, Housing) 	<ul style="list-style-type: none"> Have not received funds from provincial government (political differences) Limited in improving own-resource collection because many citizens and homes are not properly registered Limited government staff – do not have enough human resources to register citizens and help improve property tax collection
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> Successfully received funds to invest in several projects (from sectoral ministries) Have received funds from budget programs 	<ul style="list-style-type: none"> Problem: mismatch between regional responsibilities, amount of projects they oversee, and the amount of resources they receive (for own projects and for disbursements to municipalities)

⁴² Both are funds collected by the central government from rents for the exploitation of natural resources. *Canon* is regulated by national law; *sobrecanon* is regulated by special decree for each producing region.

Availability of Resources		
Municipality	Strengths	Development Areas
Coronel Portillo (P)	<ul style="list-style-type: none"> Have been able to successfully receive additional funding from budget programs Efforts with own-source revenue collection have yielded substantial budget increases (from S/. 27m in 2013 to S/. 70m in 2014) 	<ul style="list-style-type: none"> Need cultural change in citizenry so that they will pay taxes and fees for public services
Campo Verde	<ul style="list-style-type: none"> Community participation has been critical to initiating many projects – citizens provided cement and labor for a road project, for example Are continuously looking for funds from additional sources outside of budget (e.g., budget programs, funds from sectoral ministries) 	<ul style="list-style-type: none"> Own-source revenue sources extremely limited; very poor community Timing of disbursements has been a problem; have received funds that they requested early in the year by November or December, so that they do not have sufficient time to spend the funds (affects budget execution, meeting goals for additional incentive funds)
Manantay	<ul style="list-style-type: none"> Efforts with own-source revenue collection have yielded substantial budget increases (doubled) through organizing cadaster, <i>predio</i> Generally, SIAF has been a great tool for managing public resources, but extremely slow internet connection is a problem 	<ul style="list-style-type: none"> Feel that regional government have too many sectoral responsibilities and manage too much of the budget that should go directly to municipalities
Nueva Requena	<ul style="list-style-type: none"> Some funding from Housing Ministry, DEVIDA (Peru's Development Agency) Received funds from provincial government Solicited funds from the Regional and Local Investment Promotion Fund (FONIPREL) (no award yet) 	<ul style="list-style-type: none"> Because it is a very small community and transfers are determined by population without considering social or geographic factors, they feel that they never receive sufficient funds Do not have sufficient resources to finance all of the projects they need to complete One of the few municipalities visited that is heavily indebted (private loans)
Yarinacocha	<ul style="list-style-type: none"> Have received funding from budget programs, funds from sectoral ministries SIAF has been a great tool for managing public resources, has helped them with cash planning and budgeting 	<ul style="list-style-type: none"> Mentioned issues with timing of disbursements for some citizen security projects – expected funds by September, actually arrived in December

Public Investment Project Cycle		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Budget programs have been helpful in bringing language of results and indicators to the region 	<ul style="list-style-type: none"> Many budget programs do not address the most pressing social needs in the region, so projects must be funded using own resources They have difficulty with elaborating projects that will be sustainable beyond the investment/closing stages (for maintenance and operations costs)
Maynas (P)	<ul style="list-style-type: none"> Officials keep a bank of projects that tracks each approved and proposed project Administration uses Infobras for project management – tracks from proposal to 	<ul style="list-style-type: none"> Each administration has its own procedures for project management; when administrations transfer responsibilities to newly elected governments, there is a lot of

Public Investment Project Cycle		
Municipality	Strengths	Development Areas
	viability to approval to award <ul style="list-style-type: none"> Management has goal of obligating (not executing) 200-300% of investment budget 	wasted time trying to track down information <ul style="list-style-type: none"> Mentioned that they are avoiding lengthy project cycle process this year to implement a citizen security project – prefer to use funds from their operative budget instead
Belen	<ul style="list-style-type: none"> Local officials are able to elaborate some technical projects (water sanitation) Receive assistance from sectoral ministries in the elaboration of projects in other sectors 	<ul style="list-style-type: none"> Do not have sufficient resources to finance all of the projects they need to complete Limited as to the types of projects that they are able to elaborate/finance – many times they are not able to financially justify investments, because they are intended to improve social conditions only Problem with some types of housing, water sanitation, and stilt home removal plans: economy of community basically depends entirely on river, have not been able to prevent people from living in unsafe conditions
Mazán	<ul style="list-style-type: none"> Outsource drafting of technical dossier but have had success in winning funds for projects Have received assistance from some central level sectoral ministries to elaborate projects 	<ul style="list-style-type: none"> Having problems with several projects that were approved in previous years under the previous administration, but that cannot be completed (related to multiannual planning) Except for water sanitation/waste water project, they have difficulty elaborating projects that will be sustainable beyond the investment/closing stages (for maintenance and operations costs)
Punchana	<ul style="list-style-type: none"> Did not mention any issues or challenges with public investment cycle or SNIP Have received assistance from sectoral ministries when they elaborate certain types of projects to request funds Have successfully implemented public investment projects through budget programs with regional government (<i>Techo Digno</i>, trying to do the same with <i>Piso Digno</i>) 	<ul style="list-style-type: none"> Are not able to implement many of the projects they elaborate because of lack of funds or changing priorities
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> Most of their projects have passed the viability under the pre-investment stage (however, this has taken three years for most) Officials are very well prepared, have received a lot of capacity and skills training on SNIP from central government, USAID Multiannual perspective when government prioritizes and elaborates projects (seen in their strategic investment portfolio) 	<ul style="list-style-type: none"> Bottleneck has been created by taking away regional government's ability to grant environmental certification (given back to central government) Timing is an issue in project cycle; provided example of hospital project that took 6 years to complete, where a regional government is only elected for 4 year terms OPI mentioned lack of sustainability analysis after project close (particularly re: maintenance and operational costs)
Coronel Portillo (P)	<ul style="list-style-type: none"> SIAF has improved project cycle and interactions with SNIP entities in MEF 	<ul style="list-style-type: none"> Bottleneck of project cycle: environmental certifications; environmental impact studies must be reviewed in Lima

Public Investment Project Cycle		
Municipality	Strengths	Development Areas
Campo Verde	<ul style="list-style-type: none"> Can and do create projects within SNIP framework Receive a lot of assistance from regional OPI Had agreements with other municipality that assisted with pre-investment stage (but their projects were not prioritized) 	<ul style="list-style-type: none"> Have had problems with personnel rotation – affects continuity of project cycle Have not had success with getting funds from the Regional and Local Investment Promotion Fund (FONIPREL) (their projects have not won)
Manantay	<ul style="list-style-type: none"> Very clear process established for elaboration of projects (for pre-investment approval) Good system for management of projects being implemented (investment stage) Staff has received training on SNIP, project elaboration, technical dossiers 	<ul style="list-style-type: none"> Biggest issue arises after an approved project is awarded to a contractor: appeals process (for contractors that dispute the award) paralyzes any progress, must wait until appeal is resolved before government can start implementing the project
Nueva Requena	<ul style="list-style-type: none"> Officials are knowledgeable about SNIP procedures, regulations Mentioned they have at least three projects under consideration 	<ul style="list-style-type: none"> Officials say SNIP is too rigid a system to be beneficial for such a small, poor community Environmental impact analysis has become a bottleneck (previously approved by region, now must be done by the Environmental Ministry in Lima) Mandatory fees paid to contractors for elaborating a project's technical documents are very high (2-10% of total project value) and burdensome for a small municipality with a small budget allocation
Yarinacocha	<ul style="list-style-type: none"> Cycle has been improved by allowing OPIs to declare project viability (under certain ceilings) Officials have received training on the various requirements under SNIP (particularly on the elaboration of technical dossiers, project management, project close) 	<ul style="list-style-type: none"> Planning of collaborative projects (with other municipalities) has been difficult

Transparency and Citizen Oversight		
Municipality	Strengths	Development Areas
Loreto		
Loreto (R)	<ul style="list-style-type: none"> Working on improving coordination with municipalities Have improved indicators in some sectors (dental health, better roofs, child malnutrition) 	<ul style="list-style-type: none"> Have not been able to define appropriate indicators for some sectors (education, health) M&E system not established It was not evident from interview whether participative budget is used
Maynas (P)	<ul style="list-style-type: none"> Use participative budget Participation from civil society, NGOs, universities, citizens from their province Citizen oversight to monitor indicators: an individual from civil society is elected to follow progress, accountability town hall meets every 6 months to update community 	<ul style="list-style-type: none"> Citizen participation and oversight is limited – poor community, very rural
Belen	<ul style="list-style-type: none"> Requesting funds for a project prioritized by the community (open-air market) Have successfully met goals from most of the 	<ul style="list-style-type: none"> Citizen participation and oversight is limited – poor community

Transparency and Citizen Oversight		
Municipality	Strengths	Development Areas
	budget programs	
Mazán	<ul style="list-style-type: none"> • Mentioned changing attitudes in the community toward paying taxes and fee for public services, as they see results and benefits • Have successfully begun initiatives with private sector 	<ul style="list-style-type: none"> • Did not discuss participative budget • Problems with monitoring and evaluation, particularly as related to the amount of citizens who do not have IDs and cannot be registered in national systems
Punchana	<ul style="list-style-type: none"> • Use participative budget • Mayor holds accountability town halls • Participation from civil society organizations 	<ul style="list-style-type: none"> • Community involvement can be improved
Ucayali		
Ucayali (R)	<ul style="list-style-type: none"> • Many social gaps (indicators) have been reduced drastically in Ucayali region 	<ul style="list-style-type: none"> • Mentioned that they can do more to reach out to citizens, incentivize involvement and oversight
Coronel Portillo (P)	<ul style="list-style-type: none"> • Use participative budget • Successful example of projects for community that have achieved national objectives (technical training in auto repair, soldering, etc.; preventive healthcare in dengue fever, HIV, tuberculosis) 	<ul style="list-style-type: none"> • Issues with differences between urban and rural communities – different needs but not enough support from central level entities to address them • Comptroller General's office is delayed in proving audit reports and recommendations by one or two years • OSCE (Procurement Regulating Agency) does not coordinate with Comptroller General's office
Campo Verde	<ul style="list-style-type: none"> • Accountability town halls with mayor 	<ul style="list-style-type: none"> • Citizen participation in budgeting, planning, prioritization is weak • Issues with leadership – mayor was removed from office
Manantay	<ul style="list-style-type: none"> • All government workers evaluated under results framework • Successful example of meeting results in three areas: education (95% literacy rate; 300 students awarded scholarships for tertiary education; technical education for single mothers), citizen security (decreased petty theft crime from 80% to 40%); health (child malnutrition decreased from 48% to 40%) 	<ul style="list-style-type: none"> • Need better system for M&E – currently done with sectoral ministries, numbers do not always coincide with internal figures
Nueva Requena	<ul style="list-style-type: none"> • Citizen oversight was not discussed 	<ul style="list-style-type: none"> • Diverse citizenry – native communities do not actively engage or integrate • Citizen oversight was not discussed
Yarinacocha	<ul style="list-style-type: none"> • Use participative budget • Accountability town halls with mayor • Participation from civil society organizations, private sector 	<ul style="list-style-type: none"> • M&E of indicators has been a challenge because each sectoral ministry or agency uses its own procedures (no systematization)

Annex 3: Budget performance of Subnational Governments

The MEF has long used budget execution percentages as a measure of government performance. In previous years, increasing *canon* resources were transferred to the regions and local governments, but subnational governments were not always able to adjust their spending. For some, the percentage of non-executed budget became an indicator of the lack of capacity of subnational governments to perform their functions, and a way to argue for other ways to distribute *canon* resources. For others, it became clear proof for the need to recentralize responsibilities and resources.

The discussion about performance has shifted away from the budget execution capacity of subnational governments to the efficiency and effectiveness of public investment and what can be done to improve the capacity of subnational governments to provide public goods and services. This section examines the evidence about the capacity of subnational governments to execute their budgets and its impact on the quality and effectiveness of public investment.

MEF'S PERFORMANCE INDICATOR: BUDGET EXECUTION⁴³

From 2004 to 2013, total public spending in Peru experienced a dramatic increase, from S/. 48,000m to S/. 139,000m, equivalent to an average annual rate of growth of 12.5% – a substantive effort even for an economy that was growing at an annual rate of 7%-8%. During this period of rapid growth in public spending, the share of total public spending of regional governments remained about the same at 16%; however, their share in public investment increased from 14% to 22%. Although all three levels of government were part of this growth, local governments' resources grew faster (see Table 2). From a PFM perspective, there are three issues that deserve further attention: i) the effective share of public investment resources of regions and local governments; ii) the institutional capacity of subnational governments to manage those resources, and iii) the impact on public service delivery.

Concept	2004	% of total	2008	% of total	Growth	2013	% of total	Growth
Central Gov't	34,421	72	45,537	66	+32%	93,130	67	+171%
Regional Gov't	7,849	16	12,879	18	+64%	22,240	16	+183%
Local Gov't	5,732	12	13,162	18	+130%	23,630	17	+312%
Total	48,002		71,578		+49%	139,326		+190%

Table 2: Total public spending by level of government, 2004-2013

From 2004 to 2013, local government spending increased eightfold. Local governments invested about 60% of their resources, whereas the regional and central governments invested 35% and 11%, respectively (see Table 3). The central and regional governments are in charge of the largest public payrolls, including the army, police, teachers, and health personnel. At the end of the period, regional and local governments executed over two-thirds of public investment funds and close to half of total public spending.

⁴³ Starting in 2009 there is adequate information to determine the budget execution of regional and local governments. However, it was possible to determine the budget execution indicator for the three levels of government in 2008 from a World Bank study.

Concept	2004	% of total	2008	% of total	Growth	2013	% of total	Growth
Central Gov't	2,733	52	5,396	35	+97%	9,860	32	+261%
Regional Gov't	759	14	2,746	18	+262%	7,016	22	+824%
Local Gov't	1,794	34	7,133	47	+298%	14,435	46	+705%
Total	5,286		15,274		+189%	31,311		+492%

Table 3: Public investment by level of government, 2004-2013

Budget execution may not be the best indicator to measure performance, but it provides a basic measure of spending capacity for the final provision of goods and services to citizens. This is particularly true in Peru, where the budget indicator is also linked to an indicator of physical progress of projects. From 2008 to 2010, when *canon* resources were growing rapidly, there was good reason to focus on the low capacity of subnational governments to execute these abundant resources, as regions and local governments were executing around half of the allocated budget. However, this issue was true for the public sector as a whole, since the central government was executing just one percentage point ahead of local governments and eleven percentage points above regions (Table 4).

Concept	2004		%	2008		%	2013		%
	Budgeted ⁴⁴	Executed		Budgeted	Executed		Budgeted	Executed	
Central Gov't	n/a	2,733	n/a	9,800	5,396	55	11,915	9,860	83
Regional Gov't	n/a	759	n/a	6,300	2,746	44	8,653	7,016	81
Local Gov't	n/a	1,794	n/a	13,274	7,133	54	20,681	14,435	70
Total		5,286		29,374	15,275	52	41,249	31,311	76

Table 4: Allocated and executed public investment budget, 2004-2013

The budget execution rates for all three levels of government improved after 2010. Although the central government was still ahead with an execution rate of 83%, both regional and local governments increased drastically to 81% and 70%, respectively.

Performance differs according to level and type of expenditure, size of government, region, and year. Over the 2004 to 2013 period, regional governments improved their budget execution performance from 44% to 81%, an outcome similar to that of the central government and better than the local governments.

The proportional change in total investment became an important factor for the improvement of social and productive infrastructure and catalyzed a big transformation within the regions. Investment increased from 10% to 33% of regional governments' total expenditure. Current expenditure also grew, though at a slower pace. Consequently, regions still remain as the most important actor in the provision of health and educational services.

Regional performance. As a proxy for other regions of the country, as well as the performance of regional governments that do not receive *canon* transfers, three additional regional governments were selected as a basis of comparison. San Martin, like Loreto and Ucayali, is located in the jungle (*selva*)

⁴⁴ SIAF does not disaggregate budgets to level of government for the year 2004

region of Peru, but does not receive *canon* transfers. Tacna and Ancash are not located in the jungle region, but they both receive *canon* transfers. Tacna is a coastal region, highly developed and economically prosperous. Ancash is on the coast, but much of its territory is also in the mountain (*sierra*) region, and it lags behind in several indicators

Ucayali and Loreto have both improved public investment execution rates. Loreto in particular has taken advantage of the substantive increases in *canon* transfers. Tacna and Ancash, both mining-rich regions and beneficiaries of *canon* transfers, were also able to improve their budget execution performance (Table 5). San Martin, a non-mining region, shows completely different results. In the period 2009 to 2013, public investment execution decreased from 95% to 76%. This change may have been caused by a substantive increase in transfers (over 40%) for projects that were extremely difficult to implement, among many other reasons. After 2008, when the increase in *canon* transfers normalized, budget execution picked up in the regions. For the regional governments of Ucayali and Loreto, budget execution increased from 78% to 90%. Improvements were particularly significant in public investment, which increased from 59% in 2009 to 84% in 2013. Current expenditure execution was already high at 98% in 2009, though it slightly decreased to 97% in 2013 (Table 5).

Region	2009		2013	
	Current Expenditure	Public Investment	Current Expenditure	Public Investment
Ucayali	97%	56%	97%	84%
Loreto	98%	61%	96%	83%
San Martin	99%	95%	99%	76%
Tacna	96%	61%	94%	83%
Ancash	84%	25%	96%	99% ⁴⁵

Table 5: Budget execution of regional governments

In general, regional governments have demonstrated excellent capacity to execute their current expenditure budget, mainly associated with payroll of personnel providing basic public services. For both mining and non-mining regions, however, there remain unresolved issues over their new roles according to the decentralization process and the financing sources to fulfill them.

Local Governments. Two groups are used to differentiate between the municipalities visited in May of 2014 (sample group) and the remaining municipalities (non-sample) in the Loreto and Ucayali regions.

Budget execution performance varies between the examined regions. Although the changes in the average budget execution of local governments in Ucayali and Loreto (sample and non-sample) are not significant, changes between these two, 81% and 78%, and San Martin, 61%, are significant (Table 6). The biggest differences in execution occurred between current and investment expenditures of local governments. For all local governments, current expenditure execution averaged 85% while the average for investment was 71% in 2013. Current expenditure execution in Loreto, Ucayali, and San Martin was similar, at 87%, 82% and 83%, respectively. However, investment was similar only in Loreto and Ucayali, at 76% and 75%, versus 52% in San Martin. The difference between current and investment expenditure of local governments in Loreto was 11 percentage points while in Ucayali the difference was

⁴⁵ For 2013, the budget allocated to Ancash was reduced by more than S/. 1,000m; this explains its performance that year.

7 percentage points. In San Martin, the difference was 31 percentage points. In comparing highest and lowest performance of all local governments, the difference between the two groups was 20 percentage points in current expenditure execution and 43 percentage points for investment (Table 6).

Region	Notes	Current	Invest.	Difference	Combined Execution
Loreto	Sample Group	87%	76%	-11	81%
	Non-sample	91%	78%	-13	83%
Ucayali	Sample Group	82%	75%	-7	78%
	Non-sample	85%	80%	-5	81%
San Martin	N/A	83%	52%	-31	61%
All Local Governments	N/A	85%	71%	-14	77%
Extremes (All Local Governments)	High	98%	89%	-9	
	Low	78%	46%	-32	

Table 6: Local Governments: budget execution performance in 2013

Looking closely at these figures, it becomes clear that local governments in Peru are having more difficulty executing their public investment allocations. Considering that local governments spend over 46% of total investment, this issue has national implications. Although difficulties with budget execution affect all municipalities, it may be more severe in large municipalities where sizeable and more complex projects are approved.

Current expenditure execution performance looks better when examined separately from investment, with higher overall averages. Rates are similar for local governments in different regions, and do not fluctuate over the years as much as investment execution rates. These may be explained by the fact that these transactions include payrolls and recurring service expenditures.

Although total budget execution rates have improved over the last five years, they are still relatively low for regional and local governments. This is particularly true in public investment, where, as shown above, there is a lot of opportunity to improve performance. Three factors should be taken into account to explain the present situation: i) all local governments must improve performance, but larger municipalities need to improve more than smaller municipalities; ii) special attention should be given to large and more complex projects executed by larger local governments; and iii) since the SNIP institutional framework is the same for all local governments, many difficulties appear to arise from the uneven capacity of officials at regional and local governments.

Over the last decade, regional and local governments have been executing the majority of public investment in Peru. In accordance with their legal responsibilities (established in the Organic Law of Municipalities and the Organic Law of Regional Governments), they invest in urban infrastructure, roadways, water systems, garbage collection, public transportation, health and educational infrastructure, productive projects, and energy projects, among others. This was an unintended result linked to the legal formula to distribute the mining *canon*, associated with taxes on mining activities, forestry, and customs.⁴⁶ Because of the formula definition, resources are unequally distributed and concentrated in a

⁴⁶ The amount of *canon* is determined as 50 percent of corporate income tax paid by mining company. This share is distributed according to the following rules: i) District municipality where the resource is extracted 10 per cent; ii) Municipalities of the province where the resource is extracted 25 percent; iii) Municipalities of the department where the resource is extracted 40 per

relatively small number of municipalities and regions where, according to the law, they should be directed into public investment. Consequently, 10% of the municipalities receive 71% of the resources. For example, while the local governments of Cusco and Moquegua received S/. 1,400 per capita in 2013, Ucayali and Loreto received S/. 282 and S/. 128 per capita, respectively, and San Martin and Amazonas received nothing.⁴⁷ From a regional perspective, the impact of the *canon* resources is not as severe, but inequalities remain. According to the distribution, four regions receive 64% from the shared regional reserves. Therefore, Cusco and Moquegua received S/. 476 and S/. 485 per capita, respectively, Loreto and Ucayali received S/. 156 and S/. 143 per capita, respectively, and San Martin and Amazonas once again received nothing.

It should be noted that the distributive effects of *canon* have improved over the years thanks to new mining projects in different regions, but particularly due to GoP's efforts to compensate the non-mining regions through other type of transfers.⁴⁸

PUBLIC EXPENDITURE: RESULTS

Although issues over the distribution of canon resources between regions remain, questions regarding intraregional differences in distribution have shifted toward the evaluation of results (outputs and impacts) of public expenditure.⁴⁹ Although it is still a work in progress, the GoP, multilateral institutions, and PFM experts are trying to determine the efficiency and effectiveness of public expenditure in Peru and how to improve it.

According to the Institute of National Statistics (INEI), the Human Development Index has systematically improved over the last three decades in Peru. A large part of this change is explained by the excellent performance of the economy and its effects on personal income, but this improvement can also be explained by public expenditure by regional and local governments in critical sectors such as education, health, water systems, and housing (Graph 1). During this period the index improved from 0.580 to 0.741.⁵⁰ The following graph shows the improvements over the period 1980 to 2012.

cent; iv) Regional government where the resource is extracted 20 percent; and v) Universities in the department where the resource is extracted 5 per cent.

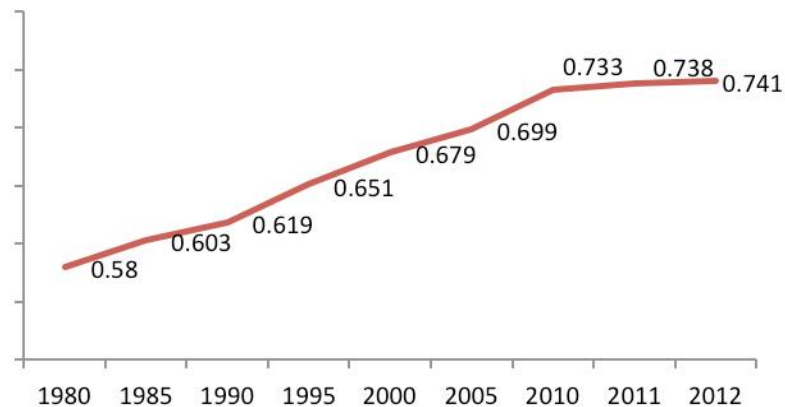
⁴⁷ *Informe Sobre Disparidades Resultado de la Distribución del Canon y Regalías*. CMMDF, 2013.

⁴⁸ *Informe Sobre Disparidades Resultado de la Distribución del Canon y Regalías*. CMMDF, 2013.

⁴⁹ See for example the recommendations of the Parliamentary Commission and a recent note in *El Comercio*.

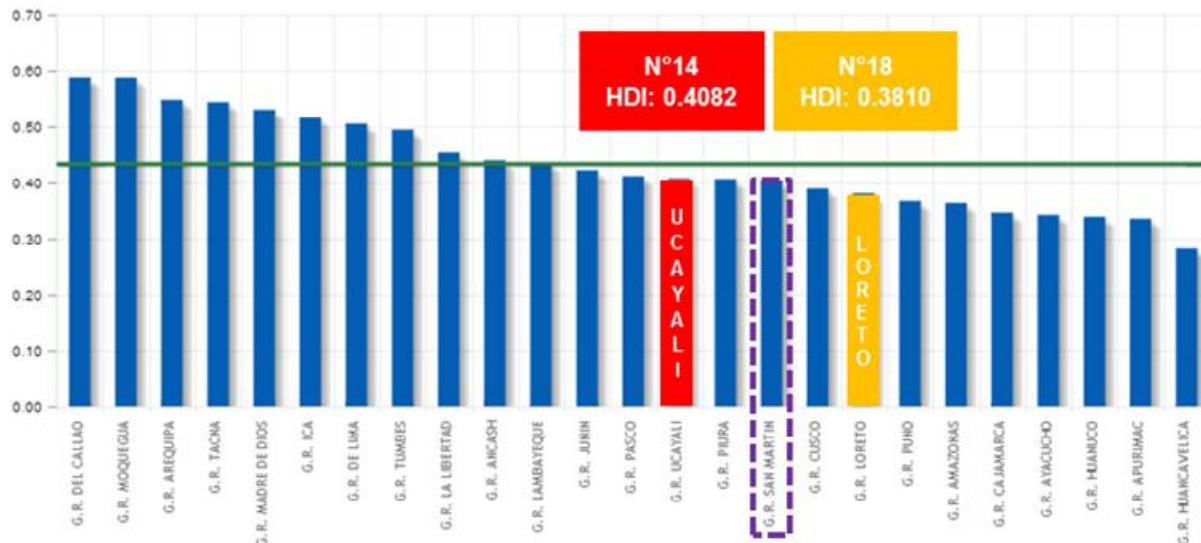
⁵⁰ Peru: HDI values and rank changes in the 2013 Human Development Report. UNDP, 2013. Available at <http://hdr.undp.org/sites/default/files/Country-Profiles/PER.pdf>.

Graph 1: HDI Composite Index for Peru



Over the last three decades, living conditions have improved in all regions of Peru, and particularly in the jungle (*selva*) region. In some cases, conditions have improved dramatically, as in San Martin and Ucayali, which have also been performing well toward meeting the Millennium Development Goals.⁵¹ As is shown in Graphs 2 and 3, all regions have also improved their Human Development Indexes; however, regions in the coast (*costa*) perform the best overall, whereas the *selva* region performs better than the mountain (*sierra*) region. Ucayali and Loreto improved between 2010 and 2012, and San Martin surpassed Ucayali by 2012. Between 1993 and 2009, levels of poverty improved in all *selva* regions, including a reduction in extreme poverty values. Loreto was the only exception, as it is the only department where extreme poverty actually increased.⁵²

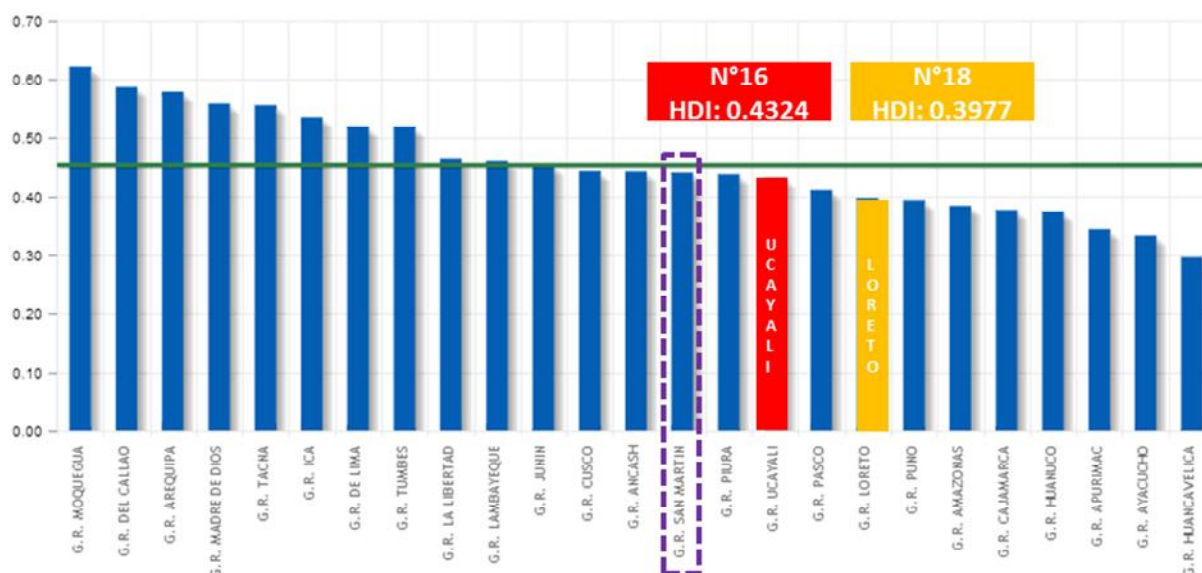
Graph 2: HDI at Regional Government Level, 2010



⁵¹ Estado de los Objetivos de Desarrollo del Milenio de la Amazonia Peruana. ARA (Articulación Regional Amazónica). 2011.

⁵² Estado de los Objetivos de Desarrollo del Milenio de la Amazonia Peruana. ARA. 2011, page 21

Graph 3: HDI at Regional Government Level, 2012



Public spending is closely related to outcomes and impact in public service delivery. Public assets and services, when they are measured by output -- that is, when they are actually being delivered -- are found to be important for reducing poverty as well as for private sector growth. This is demonstrated by a large microeconomic literature on households and firms.

CONCLUSION

All three levels of government in Peru have made substantial investments in social and productive infrastructure, as well as current expenditures. The latter covers salaries and benefits for teachers and health workers. In this sense, current expenditure is arguably more important than investment for improving social indicators. Then, the issue is to establish the efficiency and effectiveness of public expenditure and what and how to do it in order to improve both.

Although the relationship between inputs and outputs is well-known and represented through a production function, unfortunately, there is insufficient information to establish a solid quantitative linkage between public spending in Peru and the living and economic conditions of its citizens. In this vein, however, the GoP's public management reform project⁵³ is about linking inputs and results through the use of indicators. The project is still a work in progress.

A World Bank study⁵⁴ on the effects of decentralization on public expenditure efficiency in Peru states that public sector performance is determined by the amount and allocation of public resources. It examines three factors to highlight the differences in budget execution rates of regional and local governments. First, it declares that government performance and efficiency differ significantly across the

⁵³ *Programa para la Modernización de la Administración Pública*

⁵⁴ Peru: The Decentralization Process and Its Links with Public Expenditure Efficiency. The World Bank, 2010. Available at http://www-wds.worldbank.org/external/default/WDSCContentServer/WDSP/IB/2012/06/13/000333038_20120613234926/Rendered/PDF/528850ESW0P1130ation0English0final.pdf.

various regions in Peru. Second, it finds that governments in wealthier regions perform better, and governments in densely-populated areas tend to be more efficient. Third, it states that governments in resource-rich regions tend to outperform the remaining governments in all sectors, but they are less efficient.

Assuming that decentralization has had similar effects on local governments as it has on regional governments, and given that the PFM institutional framework is uniform across the country, the main explanatory factor for differences in efficiency is the disparity in institutional capacity between regions and local governments. The capacity to identify, evaluate, select, implement, and monitor and evaluate public investment helps to explain the diversity of outcomes in performance.